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Brief of Stipulation for Statement, Brief and Argument of Defendant in Error.

# Supreme Court of the United States

Filed Nov. 20, 1900.

October Term, A. D., 1900.

No. 148.

GEORGE H. SCOTT, *Plaintiff in Error,*

vs.

PARRY L. DEWEESE, (SUBSTITUTED FOR W. A. DAVIDSON) RECEIVER OF THE FIRST NATIONAL BANK OF SEDALIA, MISSOURI, *Defendant in Error.*

In Error to the United States Circuit Court of Appeals for the Eighth Circuit.

WM. H. SIMMONS,

Counsel for Defendant in Error.

IN THE

# Supreme Court of the United States

October Term, A. D., 1900.

No. 148.

GEORGE H. SCOTT, - - - - *Plaintiff in Error,*

vs.

PARRY L. DEWEESE, (SUBSTITUTED FOR W. A. LATIMER) RECEIVER OF THE FIRST NATIONAL BANK OF SEDALIA, MISSOURI, - - *Defendant in Error.*

Statement of Case by Defendant in Error.

## THE PETITION

alleges sixteen distinct facts, constituting plaintiff's cause of action, namely:

1st. The incorporation and organization of the First National Bank of Sedalia, Missouri.

2nd. The extension of the period of its succession and existence for twenty years, from October 20th, 1885.

3rd. That said First National Bank of Sedalia, Mis-

souri, from that time until its failure on the 4th day of May, 1894, continued to do a banking business.

4th. That on September 6th, 1890, said bank increased its capital stock to two hundred and fifty thousand dollars ($250,000).

5th. That on January 17th, 1891, the Comptroller of the Currency did certify that said bank had so increased its capital stock and did approve said increase.

6th. That the Comptroller of the Currency did on said 17th day of January, 1891, certify that such increase had been fully paid in as a part of the capital stock of said bank.

7th. That thereafter said bank did continue to do business on a capital stock of two hundred and fifty thousand dollars ($250,000).

8th. That on May 4th, 1894, said bank became insolvent and closed its doors and ceased to do business.

9th. That on May 10th, 1894, the plaintiff, Latimer, was appointed receiver of said bank by the Comptroller of the currency.

10th. That he duly qualified as such receiver and is engaged in winding up the affairs of said bank.

11th. That the Comptroller of the Currency of the United States afterwards determined that in order to pay the debts of said Association, it was necessary to enforce the individual liability of stockholders to the extent of seventy-five per cent. of the par value of their stock.

12th. That on April 13th, 1895, the Comptroller of the Currency made an assessment upon the shareholders of said bank for the sum of one hundred eighty-seven thousand five hundred dollars ($187,500.00), to be paid by them ratably on or before May 5th, 1895.

13th. That plaintiff made a demand upon the defendant for said assessment.

14th. That at the date of the failure and suspension of said bank, defendant was the owner of twenty-five shares of said stock of the par value of two thousand five hundred dollars ($2,500).

15th. That the plaintiff notified the defendant of said assessment and requisition of the Comptroller of the Currency and demanded payment of the same.

16th. That the defendant has not paid said assessment. (Admitted by answer as there is no plea of payment).

## THE ANSWER

contains the following specific admissions of the allegations of the petition, namely:

1st. Admits the incorporation and organization of the First National Bank of Sedalia Missouri.

2nd. Admits the extension of the period of its existence.

3rd. Admits that it continued to do a banking business as alleged in the petition.

4th. That said bank became insolvent and closed its doors as alleged in the petition.

5th. That the plaintiff was appointed receiver of said bank on the 10th day of May, 1894.

6th. That he duly qualified as such receiver and is now acting as such.

7th. That the Comptroller of the Currency determined it was necessary to enforce the individual liability of its stockholders to the extent of seventy-five per cent. of the capital stock held by them.

7½. Admits that the Comptroller determined that it was necessary to collect from them, ratably, the said amount of seventy-five per cent. of the par value of the stock held by them.

8th. That a demand was made upon the defendant for his pro rata share of said assessment and directions given to the plaintiff Latimer to enforce the payment of said amount.

6th. That on September 6th, 1890, by a vote of the owners of two-thirds of the capital stock of said bank, its capital stock was increased one hundred and fifty thousand dollars ($150,000).

10th. Admits that said bank notified the Comptroller of the Currency that the whole amount of said increase had been paid in.

11th. Admits that on January 17th, 1891, the Comptroller issued his certificate stating that the amount of the increase of the capital stock was one hundred and fifty thousand dollars and that the same was paid in.

12th. That thereafter said bank continued to do business with the capital stock of two hundred and fifty thousand dollars.

13th. That defendant subscribed for twenty-five shares, aggregating the sum of two thousand five hundred dollars ($2,500), of said capital stock and received his certificate for the same.

14th. Admits that plaintiff received eighteen per cent. of the par value of said stock from said bank as dividends thereon.

### Allegations of New Matter in Answer.

After these admissions, the answer sets up the following new matter as a defense to the cause of action set forth in the petition:

1st. That at the time the Comptroller issued his certificate stating that the capital stock had been increased one hundred and fifty thousand dollars ($150,000), and that the sum had been fully paid into said bank, said Comptroller of the Currency knew that more than the entire capital stock of said bank was then loaned to its president, and that the amount so loaned had been constantly increasing for several years up to January 17th, 1891, by adding the interest to the principal.

2nd. That the Comptroller of the Currency based his

action in issuing his said certificate as to the increase of said capital stock, wholly upon the notification of said bank that said increased capital stock had been subscribed and fully paid in.

3d. That in September, 1890, the officers of said bank informed and represented to defendant that it contemplated increasing its capital stock from one hundred thousand dollars ($100,000) to two hundred and fifty thousand dollars ($250,000). That such increase was desirable on account of the increasing business of said bank, which was in a flourishing condition and earning large dividends, and that it had a surplus of fifty thousand dollars ($50,000) over and above its capital stock and all liabilities; and that from said surplus such dividends would be declared as would make said increased shares worth one hundred and eight dollars ($108) per share; that said representations were false and defendant was deceived thereby, and that relying upon the same he subscribed for fifty share of said increased capital stock; that he paid said bank for said twenty-five shares the sum of five thousand four hundred dollars ($5,400), and on or about October 25th, 1890, he received from said bank fifty shares of said increased capital stock. That said bank then falsely and with intent to deceive defendant, represented that the said increase of capital stock had been lawfully made and that the full amount thereof had been subscribed for and paid in in full; and that defendant deceived by said representations, accepted and retained his said certificate of stock *and has received dividends thereon aggregating eighteen per cent. of the par value of said certificate*, which dividends were paid out of the money paid as aforesaid by defendant to said bank.

4th. That in September, 1890, and for a long time prior thereto and ever afterwards, said bank was wholly

insolvent and at the time said pretended increase of capital was made, all of the capital stock of said bank had been lost and its liabilities irrespective of its capital stock and alleged surplus, exceeded its assets; and that it was earning no dividends upon its capital stock. And that said pretended increased stock was never of any value or validity, *and that only about two-thirds of said increase was ever paid in;* and that the officers of said bank made false entries in the books and records of said bank for the purpose of showing *an apparent surplus and declared a dividend to themselves therefrom, and turned in said dividend to the bank in pretended payment for a large part of said increased stock*; that said increase stock was a sham and done for the purpose of bolstering up an insolvent institution and for the purpose of watering the capital stock of said bank and permitting the officers thereof to appropriate to themselves without paying therefor, a large part of said pretended increase, and that defendant had no knowledge or suspicion of this state of affairs until said bank closed its doors on the 4th day of May, 1894.

5th. That the books and records of said bank during all the time after said October 25th, 1890, have shown, and it was made by them to appear that all of said increase was paid in, and were so systematically and cunningly falsified by said officers, that defendant could not by the utmost diligence ascertain the true condition of said bank; and that defendant, as soon as he discovered that said increase was not fully paid in, disclaimed and denied that he had ever been a stockholder of said bank; that at all of the times stated said bank and the officers thereof, had full notice and knowledge that all the representations made by said bank were false and fraudulent.

**Analysis of Allegations of New Matter.**

After thus analyzing the petition and the answer, it will be seen that all the allegations of the petition stand admitted, and that the only legal question involved in the case now is, whether the new matter alleged in the answer constitutes any defense whatever, to the cause of action set up in the petition.

The allegations of new matter may be analyzed as follows:

1st. That at the time the Comptroller of the Currency issued his certificate that the capital stock had been increased to two hundred and fifty thousand ($250,000), and that the one hundred and fifty thousand dollars ($150,000) of increased capital stock had been paid in, he knew that the entire capital stock of one hundred thousand dollars ($100,000), had been loaned to the president of said bank and the interest had been added to the principal for several years.

2nd. That the Comptroller had based his action in so certifying wholly upon the notification of said bank that its capital stock had been so increased, and the increase fully paid in.

3rd. False and fraudulent representations of the officers of said bank as to its financial conditions, its surplus and dividends, and as to the increased capital stock, having been subscribed for and fully paid in, by which defendant was induced to subscribe for his stock.

4th. That when said increase was made, said bank was insolvent and its capital stock lost.

5th. That only about two-thirds of said increased stock had ever been paid in.

6th. That the officers of said bank made false entries in its books, showing an apparent surplus from which to

declare a dividend, and then turned in said dividend in pretended payment for a large part of said increased stock.

7th. That the books of said bank were falsified, so that defendant could not, by diligence, ascertain the true condition of said bank, and that as soon as he did discover it, he disavowed being a stockholder.

8th. That defendant did not ascertain the true condition of said bank, until after it failed, and that as soon as he discovered that said increase had not been fully paid in, denied that he had ever been a stockholder.

FROM THE FOREGOING STATEMENT IT WILL BE SEEN,

1st. That the answer DOES NOT ALLEGE that the whole of the $150,000 increase of capital stock had not been in good faith SUBSCRIBED, but only that it HAD NOT BEEN FULLY PAID FOR.

2nd. That this failure to pay, was not the result of any refusal of any of the subscribers to this increased stock to pay, but because a part of the subscribers paid a part of their subscription, in dividends, which had been declared by the bank in their favor, and which dividends it is now alleged, four years after they were declared, were not in reality due them, and hence their stock was not *fully paid for.*

3rd. That the answer does not offer to rescind the alleged "contract" of subscription, nor does it offer to return the dividends received, aggregating 18 per cent of the par value of the stock, nor to account for it.

IT WILL ALSO BE NOTICED that whilst he alleges that he *could not* have ascertained that the bank books had been falsified by the "*utmost diligence,*" yet he does not allege that he exercised any diligence whatever, or that he made any inquiries, whatever, or that he even attempted to learn the true state of the accounts of said bank *before* he subscribed

for his stock, nor *afterwards before the bank failed*, nor does he state any facts showing why he was so easily and quickly able to ascertain their falsified condition so soon *after* the bank failed, when, by the "utmost diligence he could not ascertain the true state of the bank," *for nearly four years before it failed.*

The averment that he could not, by the utmost diligence, ascertain the true state of the bank is a mere conclusion, and is not tantamount to an averment that he exercised diligence.

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**Decision in U. S. Circuit Court.**

It is true, that in the United States Circuit Court for the Central Division of the Western district, of Missouri, no opinion was written or filed in this particular case, but there were a large number of cases, all involving the same questions, consolidated, and the opinion was written and filed in the case of *Latimer* vs. *Bard*, in which a demurrer was filed to the answer, instead of a motion for judgment upon the pleadings.

The opinion of Adams, Judge, in that case, reads as follows:

(See 76 Fed. Rep. p. 536.)

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**Opinion in U. S. Circuit Court.**

"The several cases consolidated into this action are brought by the plaintiff as receiver of the First National Bank of Sedalia, against divers persons, stockholders of said bank, to recover the amount of an assessment made by the Comptroller of the Currency of 75 per cent. of the stock held by them respectively. The defendants file a joint answer, setting forth in effect that the stock held by them upon which such assessment was made is part of a

pretended increase of stock, that such increase was invalid and unlawful, for the reason, as alleged, that the whole amount of such increase was not paid in. It appears by the answer, that the original capital of the bank was $100,000: that on September 6, 1890, the shareholders by a vote of the owners of two-thirds thereof, resolved to increase the capital in the sum of $150,000, so as to make it $250,000, instead of $100,000, as theretofore; that subsequently certificates for the increase were issued to the subscribers therefor; that thereafter on January 17, 1891, the Comptroller of the Currency of the United States duly certified that said bank had increased its capital in the sum of $150,000, with his approval thereof, and further certified that the whole amount of such increase had been paid in. It further appears that the defendants received the certificates representing the stock subscribed and paid for by them prior to October 25, 1890; that during the years 1891 and 1892 the defendants, as such stockholders, received dividends on their stock amounting in the aggregate to 18 per cent. theroof; that, notwithstanding the apparent conformity with all the provisions of the acts of Congress, relating to the increase of stock, in point of fact, at least one-third of the amount of such increased stock was subscribed for by the officers of the bank, who subsequently issued certificates to themselves therefor, without paying anything for the same; that this was accomplished in the following way and manner, as stated in the answer as amended, that is to say:

'By fictitious and false entries entered in the bank books and records they made a showing of an apparent surplus in the bank's assets for division among themselves as holders of the original capital stock, and went through the form of declaring a dividend therefrom to themselves, and returning the same to the bank as an alleged payment for their shares of the increased

stock, whereas no money passed, the whole transaction was a mere sham, there was no surplus (the bank being then insolvent),—and all of which was done with the fraudulent purpose on the part of said officers of appropriating to themselves a part of the increased stock without any payment thereof. All of which was done without the knowledge or consent of any of the defendants, none of them having any knowledge thereof until after the making of the assessment sued on.'

It is further alleged in the answer that no profits were made by the bank after the defendants subscribed for the increased stock, and that the dividends which they received as stated, were paid to them out of the capital which they had paid in; that the officers of the bank falsely and fraudulently represented to the defendants, at the time of taking their subscriptions and receiving their money, that the bank was solvent, that the increase had been lawfully made, and that the same had been fully paid in, that these statements were false, and known to be false by the officers of the bank when making them; that the defendants made their subscriptions and paid in the amount thereof and took their certificates in implicit reliance upon such statements; that the defendants had no knowledge of the falsity thereof, or of the false entries made as aforesaid, or of the alleged illegality of the increase of stock, until after the Comptroller of the Currency made the assessment against the stockholders on April 13, 1895, and by the exercise of ordinary care could not have discovered or known the truth; that immediately on discovering the facts, after the assessment was made against them, they tendered to the plaintiff the amount received by them as dividends as aforesaid, and offered to deliver up their stock to him, also. To this answer a demurrer is interposed. The defendants' counsel do not rely upon the false representations as such of the officers of the bank, as a defense, but, in argument, contend solely that the increase of capital was void because the whole

amount of such increase was not in good faith paid in, and that defendants are entitled to invoke such fact as a defense to this action against them.

The only question for consideration, therefore, is whether or not the alleged fraudulent action of the officers of the bank in figuring out an apparent surplus entitling them as holders of the original stock to a dividend, and appropriating the same to themselves and using it in paying up their quota of the increased stock, rendered invalid and void the entire increase. The national banking law (section 5142, Revised Statutes, 1878), and the amendment of May 1, 1886, (24 Stat. 18). provide, in effect, that three facts must concur to constitute a valid increase of the capital stock of a national banking association: First, a vote of shareholders owning at least two-thirds of the original capital; second, the whole amount of the increase must be paid in; third, the Comptroller of the Currency, by his certificate specifying the amount of increase of such capital, must approve thereof, and certify to the fact of its payment. The pleadings in this case show the requisite vote of shareholders and the requisite certificate of the Comptroller. The case shows by fair inference from the facts pleaded and law necessarily applicable thereto, that the bank, by and through its proper officers, advised the Comptroller, among other things that the increased capital had been duly paid in. Acting upon this advice, and such other information as to him seemed requisite, the Comptroller approved the increase, and made the necessary certificate that the amount of the increase had been duly paid in as part of the capital of the banking association.

1. If there was nothing else in this case, I would hold that the action of the Comptroller, as last stated, is conclusive of the question of fact certified by him, and that the

defendants are not at liberty, in this collateral proceeding, to open the same. The comptroller occupied a position quasi judicial in its character. His finding and certification of the fact now in question was an exercise of the judicial function, and ought not to be disturbed except upon some appropriate direct proceeding to that end. In the case of Casey v. Galli, 94 U. S., 673, the receiver of a national banking association sought to recover from a stockholder the amount of an assessment duly made by the Comptroller. The stockholder, among other defenses, set up the fact that the banking association was created under the provisions of the national banking law permitting a state bank to be converted into a national bank, and that two-thirds of the capital stock never authorized the conversion and never accepted the organization certificate, as required by the act of Congress, as conditions precedent to such conversion. Section 18 of the act provides that when the Comptroller shall give to such association a certificate under his hand and official seal that the provisions of the act have been complied with, and that it is authorized to commence the business of banking under it, the association shall be deemed to be a national banking association, the same as if originally organized under the act. The Supreme Court, in passing on the case, says:

'The plea denies the irregularity of the proceedings in the single particular that the owners of two-thirds of the capital stock of the bank did not authorize the directors of said bank to convert it into a national banking association nor to accept an organization certificate as such banking association.'

After alluding then to the admission contained in the pleadings that the Comptroller's certificate was duly made, the Court says:

'The plea proposed to go behind the certificate and contradict it. This cannot be done. The Comptroller was clothed with the jurisdiction to

decide as to the completeness of the organization, and his certificate is conclusive upon the subject for all purposes of this litigation. It has the same effect, and for the same reason, as his determination and order with respect to the amount to be collected from such stockholders in the event of the failure of the association. No question can be raised in this collateral way as to either. In Thatcher v. Bank, 19 Mich., 196, it is held 'that whether there was any defect in the process of organization was a question for the Comptroller to decide, and that his certificate of compliance with the requirements of the act of Congress removes any objection which might otherwise have been made to the evidence upon which he acted.' In this we concur.'

The case of Smelting Co. v. Kemp, 104 U. S. 636, is a leading case on the conclusiveness of the findings of executive officers of the government upon matters referable by the law to them. In the opinion in the last mentioned case it is said:

'In that respect they [officers of one of the executive departments] exercise a judicial function, and therefore it has been held in various instances by this Court that their judgment as to matters of fact properly determinable by them is conclusive when brought to notice in a collateral proceeding. Their judgment in such cases is, like that of other special tribunals upon matters within their exclusive jurisdiction, unassailable except by a direct proceeding for its correction or amendment.'

To the same effect, also, are the cases of Barden v. Railroad Co., 154 U. S. 288, 14 Sup. Ct. 1030, and U. S. v. Winona & St. P. R. Co., 15 C. C. A. 96, 67 Fed. 948.

Applying the principles of the foregoing cases, it seems to me clear that the action of the Comptroller of the Currency in certifying that the whole amount of the increase of stock had been paid in, with his approval of the increase, so partakes of the judicial character that it cannot be assailed in this proceeding. In reaching this conclusion it must be borne in mind that the particular matter which, by the answer, is relied upon as a defense, is, by the act of Congress, pointedly referred to the Comptroller for his

finding and certification. If, therefore, the finding of any executive officer of the government, in any case, is to be treated as conclusive (except as against direct attack), it seems to me his finding and certificate of this fact ought to be. The important and diverse business interests of a bank, and the welfare of its stockholders and creditors, demand, in my opinion, that a matter of fact so affecting each and all of these features as the stockholders' relations to the bank, and their liability to its creditors, should be fixed, clearly and definitely, by some decisive authority, and this is what I think Congress undertook to do in requiring the Comptroller of the Currency to find and certify to the fact in question, and as a result thereof to give his approval to the increase. The foregoing is decisive of the demurrer in this case, but as other important and grave questions have been argued by counsel I will briefly advert to them.

2. The pleadings, as already seen, show that the defendants received their certificates of stock and became ostensible shareholders prior to October 25, 1890. From and after that date, at the latest, the bank was held out to the world as possessing a capital of $250,000, and these defendants allowed themselves to be held out as shareholders of the bank, and, under the law, as liable to creditors to the extent of the amount of stock held by them. It is a matter of common knowledge, and goes without saying, that the double liability of shareholders in national banks is relied upon by creditors as security for their debts. Relying upon this security, depositors trusted the bank, and it became indebted to divers persons in such large amounts that at least 75 per cent. of the capital stock (besides all the other assets of the bank) is required to pay them. The ostensible relation of the defendants to the bank and its

creditors was, for five years, that of shareholders. By their conduct they influenced persons to their injury. They ought, therefore, unless some controlling principle of law is violated, to be held to the liability to which they have apparently been subject. But it is said that they are not bound because they did not know the facts relied upon now as a defense until the failure of the bank, and after the assessment was made by the Comptroller against them, and because they could not, by reason of the fraudulent conduct of the officers of the bank, by the exercise of ordinary care, have ascertained such facts sooner. I do not think they can be heard to excuse themselves in this way. They ought to have been more diligent in ascertaining and knowing the facts. They had enjoyed all the privileges of stockholders in corporations of this state, including the full right of personal examination and inspection of books, papers, and documents. They admit that they did, in fact, discover the truth after they were called upon to respond to their apparent liability. This admission shows that the discovery was not only possible, but that when their financial interests required attention they were able to discover the facts of the case. In my opinion they ought to have seriously considered this subject when the financial interests of the bank's creditors required attention.

In the case of Upton v. Tribilcock, 91 U. S. 45, it is said:

'The principle laid down in the charge of the Judge, that one who claims to have been drawn into a fraudulent purchase must exercise care and vigilance to discover the fraud, and must be prompt in repudiating his contract on the ground of such fraud, is a sound one. * * * A party must use reasonable diligence to ascertain the facts. * * * Parties who are shareholders, and claim to be relieved on the ground of fraud, must act with the utmost diligence and promptitude.'

Applying the foregoing principles to the facts before

the Court in that case, the Supreme Court held as follows:

'To subscribe for stock in a corporation in August, 1870, to rest quietly until the year 1873, never making any investigation as to the position in which he stood until that time, and until after the assignee in bankruptcy had made a demand upon him, falls very short of what the law requires. * * * It was his plain duty to have inquired and to have ascertained his position long before he did.'

To the same effect is the case of Sanger v. Upton, 91 U. S. 64, where it is said:

'She [the shareholder] was estopped from denying her ownership; she could not assert her title if there were a profit and deny it if there were a loss.'

No more can these defendants be allowed to deny their ownership of the stock in question after having taken their certificates, asserted their ownership, and received dividends, in times of prosperity. They allowed five years to elapse, and during this period received profits from the conduct of the business of the bank, permitted debts to be contracted on the strength of their apparent liability under the law for their payment, and their only answer now is that they could not have discovered the alleged fraud by the exercise of 'ordinary care.' Greater care and diligence than this was required of them. They are therefore estopped by their own laches from denying the liability now asserted against them.

3. Again, the officers of the bank, in taking the necessary steps for increasing its stock, acted as the agents and trustees of the parties interested in such increase. Their acts are the acts of their principals, and while they may be held to individual liability to their cestuis que trustent for breaches of their trust, neither they nor their principals ought to be heard to assert their own wrong to defeat the claims of innocent third parties who acquired rights upon the faith of what was apparently done. Under such cir-

cumstances the equities of creditors are greater than those of defrauded principals even, and to permit such principals now to deny their liability would defeat the ends of justice and work a legal wrong. Ogilvie v. Insurance Co., 22 How, 380; Railway Co., v. McCarthy, 96 U. S. 258; Bank v. Hawkins, 18 C. C. A. 78, 71 Fed. 371; Duffield v. Iron Works, 64 Mich. 292, 31 N. W. 310.

4. It is further argued by defendants' counsel that the entire increase of stock in question was ab initio void, and hence that no question of estoppel can arise against the defendants in this case. They say it was ultra vires and void because one of the essential and statutory requirements was not complied with, namely, 'the whole amount of the increase was not paid in.' They contend that the paying in of the whole amount of the increase was a fundamental prerequisite to a lawful and valid increase, and that the failure so to have done, as pleaded by defendants, renders the increase absolutely void. This argument proceeds entirely upon the alleged want of power in the bank. Notwithstanding the views already expressed concerning the conclusiveness of the Comptroller's certificate, I will briefly consider this view of the case.

Counsel rely mainly on the cases of Winters v. Armstrong, 37 Fed. 508, and Delano v. Butler, 118 U. S. 634, 7 Sup. Ct. 44, in the last of which the Supreme Court says:

'It appears that three things must concur to constitute a valid increase of the capital stock of a national banking association: First, that the association, in the mode pointed out in its articles and not in excess of the maximum provided for by them, shall assent to an increased amount; second, that the whole amount of the proposed increase shall be paid in as a part of the capital of such association; and, third, that the Comptroller of the Currency, by his certificate specifying the amount of such increase of capital stock, shall approve thereof and certify to the fact of its payment.'

This language was used prior to the amended act of May 1, 1886, and would necessarily be somewhat modified now, if treating of the same subject under the provisions of the amended act, but for all the purposes of the argument in question this circumstance is immaterial. The argument is that these three several requirements are expressions of limitations upon the fundamental power conferred upon the bank to increase stock, and that the failure to comply with either of these requirements, in an attempted increase, renders the consummation void for want of fundamental authority therefor. It must be conceded at the outset that if the sovereign authority never conferred power upon the bank to increase its stock at all there was no valid increase in this case, no valid subscriptions by the defendants to such increase, and no liability on their part by reason of any certificates therefor which they may have received; and in such case no acquiescence, laches or estoppel on the part of the defendants, as subscribers to such stock, can work any liability against them. Scoville v. Thayer, 105 U. S. 143; Implement Co. v. Stevenson, 13 C. C. A. 661, 66 Fed. 633. Inquiry must therefore be first made as to whether the requirement that the whole amount of the increase must be paid in relates to the abstract power to increase, or to the performance of that power.

Section 5142, Revised Statutes, 1878, provides as follows:

'Any association formed under this title may, by its articles of association, provide for an increase of its capital from time to time, as may be deemed expedient, subject to the limitations of this title. But the maximum of such increase to be provided in the articles of association shall be determined by the Comptroller of the Currency; and no increase of capital shall be valid until the whole amount of such increase is paid in, and notice thereof has been transmitted to the Comptroller of the Currency, and his certificate obtained specifying the amount of such increase of the

capital stock, with his approval thereof, and that it has been duly paid in as part of the capital of such association.'

This section was amended by the act of May 1, 1886, (24 Stat. 18). The first section of this amended act reads as follows:

'That any national banking association may, with the approval of the Comptroller of the Currency, by the vote of shareholders owning two-thirds of the stock of such association, increase its capital stock, in accordance with existing laws, to any sum approved by said Comptroller, notwithstanding the limit fixed in its original articles of association and determined by said Comptroller; and no increase of the capital stock of any national banking association either within or beyond the limit fixed in its original articles of association shall be made except in the manner herein provided.'

In considering the question of 'abstract power,' it is well at the outset to clearly understand what is meant by the expression. It is said in the case of Bank v. Hawkins, 18 C. C. A. 80, 71 Fed. 370:

'An act is ultra vires a corporation when it is beyond and outside of the scope of the powers conferred by its founders, when the corporation is without authority to perform it under any circumstances or for any purpose.'

In other cases it is held, and it is generally so understood, that, if any way is provided by law for accomplishing a desired purpose, power in the abstract may be said to exist for doing it.

The statutory provisions above quoted undoubtedly provide some way for increasing the capital stock of a national banking association and certainly authorize the increase under certain circumstances and subject to certain requirements. They therefore provide 'abstract power,' as already defined, for doing the act. The steps to be taken in effecting the increase are enumerated in the acts, but these, with the exception of the approval of the Comptroller of the Currency, do not in my opinion concern the question of abstract power to do the act, but relate exclusively to

the method of performance or the exercise of the power granted. Scoville v. Thayer, *supra*, was an action to recover an unpaid balance due on subscription to increase stock. According to the laws of Kansas, where the corporation there under consideration was organized, any corporation might increase its stock to any amount not exceeding double its authorized capital. After exhausting this power in making one increase which fully doubled its authorized capital, the corporation attempted, by taking the steps required by law for the lawful increase of stock, to further increase its capital. The Supreme Court held that this attempted second increase presented a clear case of want of power in the abstract, which no acquiescence laches, or estoppel could cure.

Implement Co. v. Stevenson, *supra*, presents another instance of total want of power to make the increase. An attempt was made here to increase stock of a corporation to an amount in excess of the statutory limit, and the Circuit Court of Appeals followed the doctrine of Scoville v. Thayer, but in the opinion drew a sharp distinction between that case and others, involving a defective or informal exercise of the power granted, holding that in the latter case a stockholder may estop himself from denying the validity of the stock or his liability therefor.

Veeder v. Mudgett, 95 N. Y. 295, is a case in which the Court of Appeals of New York, says: 'The abstract power [to increase the stock] did exist, and there was a way in which the increase could lawfully be made, and the creditors could without fault believe that the increase had been lawfully effected, and the necessary steps had been taken,'—and holds, notwithstanding failure to comply with certain requirements of the statute relating to increase of capital stock, that the stockholders, by voting for such

increase, accepting their proportion of it, and dividends upon it, and by holding it out as a component part of the capital, are estopped from denying the legality of the increase.

In Chubb v. Upton, 95 U. S. 665, it appears that the holders of the original capital stock never authorized the increase, and other such irregularities occurred as, between the stockholders and the company, might have subjected the increase to annulment by a direct proceeding; yet the Court says:

'All this does not alter the fact that there was an attempted alteration of the company, under the form of law, approved by the attorney-general, with an increased capital, in the organization and management of which the defendant took part; that he paid his money, received his certificate of stock, attended meetings, voted, acted as an officer, and, so far as the record shows, never repudiated his position at any time, even to the time of the trial. If successful, he would have shared in its profits. He may have been the dupe and victim of the actions of others; he may have been an a complice; at all events he was so far an actor in the affair that he cannot escape the consequences of his position.'

As a result of a careful examination of all the cases bearing on this question, I am constrained to hold that the statutes of the United States confer the abstract power upon national banking associations to increase their capital to such a limit as might be approved by the Comptroller of the Currency, and that this power, as such, exists independently of the separate steps required to be taken by the shareholders in the exercise of the power, and that any irregularities, informalities, or defects in the exercise of the general power, like that set up as a defense to this action, may be waived by the subscriber; and that the defendants in this case, by their laches and conduct, have so waived it, and are estopped from availing themselves of the irregular-

ity complained of by them. The demurrer must be sustained."

In the Circuit Court many points were raised and discussed, but in this Court, the plaintiff in error raises but two, to-wit:

1st. That there was no valid increase of capital stock made, because the whole amount of the proposed increase *was not paid in.*

2nd. That plaintiff in error is entitled to a recision of his subscription contract.

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## Brief and Argument.

### I.

The certificate of the Comptroller, approving the increase of capital stock and certifying that it had been fully paid in, is conclusive, and the validity of the increase cannot be assailed in a collateral proceeding like this.

*Latimer vs. Bard, 76 Fed. Rep. 536, and cases cited.*

Bailey vs. Sellinghost, 99 Fed. 801.

To the same effect, or, involving the same principle, see—

*Sheafe vs. Larimer, 79, Fed. Rep. 921.*

This is so held with reference to the Comptroller's action, in making an assessment against stockholders.

*Kennedy vs. Gibson, 8 Wall, 498.*

*Casey vs. Galli, 94 U. S. 673.*

*Nat. Bank vs. Case, 99 U. S. 628.*

And with reference to his action in certifying that a banking association is duly organized, and entitled to commence business;—

*Casey vs. Galli, supra.*

*Latimer vs. Bard, 76 Fed., 536 on 539.*

If these cases be correctly decided, the principle therein established cuts off all further discussion of this case.

But we propose to go a step further. and show that even if this case was not dominated by this principle, yet the new matter set up in the answer does not constitute a defense to this action.

II.

The first defense is, that when the Comptroller issued his certificate, certifying that all of said increased stock had been paid in, as required by Sec. 5142, Revised Statutes, U. S., 1878, that only about two-thirds of it had in fact been paid in, and that for this reason the increased stock was invalid, and Scott being entitled to a recision of the contract of subscription, is not liable for this assessment.

Counsel for defendant in error, might well be content with referring this Court, upon this point, to the able opinion of the United States Circuit Court of Appeals, rendered in this case, and printed in the transcript of the record, pages 19 to 32 inclusive.

It would scarcely be possible to *refute* the doctrine contended for by plaintiff in error, in more clear or stronger language than is used by JUDGE SHIRAS in that opinion.

And we beg leave to call this Court's attention to the fact that Judge Shiras' opinion *supra*, was evidently written under the impression that *no sort of payment whatever* was ever made for about one-third of the increased stock, whereas the answer shows that it was *paid for in full*, but that a part of it was paid for in dividends declared from a *surplus*, which plaintiff in error *now says, did not exist.*

The bank declared these dividends. It accepted them in part payment for the increased stock, and it certified to the Comptroller that the whole amount of such increased

stock had been paid for in full. How can the plaintiff in error, in this collateral action, be permitted to go back to a time *four years* before the bank failed, and about *six years* before this action was brought, and inquire into the fact as to whether such surplus did exist, and upon the determination of that fact, assert that the stock was or was not paid for?

We beg leave, however, to suggest that this exact point, decided by Judge Shiras, was long before considered, and decided adversely to the contention of plaintiff in error, in each of the following cases, to-wit:

*Latimer vs. Bard, 76 Fed. Rep., 536.*
*Winters vs. Armstrong, 37 Fed., 503.*
*Vedder vs. Mudgett, 95 N. Y., 295.*
*Stutz vs. Handley, 41 Fed. Rep., 531.*
*Aspinwall vs. Butler, 133 U. S., 234.*
*Butler vs. Eaton, 141 U. S.* 240.

The objection to the argument of the learned counsel for defendant is the effect they give to the statute. The amended act quoted and which governs the increase of capital stock in national banking associations, clearly confers the power upon such associations to increase their capital. It says: "That any banking association may, with the approval of the Comptroller of the Currency, by the vote of shareholders owning two-thirds of the stock of such association, increase the capital stock in accordance with existing laws."

Here is clearly given the *power* to make the increase, subject only to the approval of the Comptroller. The manner of making the increase is provided, that is by a vote of shareholders owning two-thirds of the stock.

But the same section further provides that no such

increase "shall be made except in the manner herein provided." We agree with the counsel for defendant that this amendment does not repeal the other requirements of the original act and that that part of the original section, to-wit:

"And no increase of the capital shall be valid until the whole amount of such increase is paid in," should be held as part of the act in force.

The question is what effect has this clause in cases where the banking association has in all respects complied with the requirements of the statute except to pay in the increased capital, and the owners of such stock have accepted it, voted it and accepted dividends thereunder.

The intention of the legislature must always be sought after in deciding upon the legal effect of words contained in a law or charter, and unless it appears affirmatively that the legislature intended to render a forbidden act absolutely void in legal contemplation, it will not be so held.

To adopt the construction contended for by the defendant, is in effect to declare that under this statute, although subscribers may receive their stock, and derive from it all the resultant benefits for years, yet when the burdens which accompany the ownership fall upon them, they may repudiate their contract, pleading as a defense thereto their own wrong.

The Courts do not so hold and the cases cited by counsel for the defendant do not support his contention. The expression of the Court in the case of Delano vs. Butler, *supra*, relied upon, is not construed in the subsequent cases as counsel for defendants contends, as a review of them will disclose.

The case of Winters vs. Armstrong, 37 Fed. Rep. 508, arising out of the failure of the Fidelity National Bank of

Cincinnati, was a case in which none of the requisite steps were taken to increase the capital stock and in the discussion of the liability of the subscriber in that case, Mr. Justice Jackson considers the very question raised in this case. On page 518 the learned judge quotes from the case of Scoville vs. Thayer, showing that in that case the corporation had authority by law by its own act to increase its capital stock to a certain limit, but when it passed that limit the increase was in excess of its prescribed authority and was wholly wanting in legal validity and hence no act of the corporation, or acquiescence of the subscriber could operate to give the subscription validity or estop the shareholder, even in favor of creditors. Then the Court continues:—

"National bank associations have no authority of law by their own action to increase their capital stock to any amount whatever. They can make no increase to any extent without the approval of the Comptroller as the representative of the government. His approval confers the right to make and fixes the limit or the amount of such increase. Within its own power and by its own action a national bank can make no increase of its capital stock. It might, and would doubtless be, true that with or after the Comptroller's approval of an increase, which involves the exercise of discretion, supervisory on his part, and wholly beyond the control and independent of the action or wish of the association or of its stockholders, the steps taken or mode of procedure adopted by the bank might not strictly conform to the requirements of the law; that for want of such conformity the action on the part of the association might be illegal; and that the *stockholders or subscribers for such stock*, who had accepted an alotment of shares thereunder, and acquiesced in the steps taken and the proceed-

ings had by the association in the preliminaries to be performed on its part, *would be bound.* In effecting an increase of its capital stock the association may, so far as relates to its own action, proceed in an irregular or informal manner, which a stockholder *who has acquiesced therein may not, as against either the corporation or its creditors, take advantage of or insist upon as invalidating his subscription, or the stock issued to him thereunder.* But in regard to the sovereign's consent to increase, to be expressed in and by the approval of its Comptroller of the Currency, that is an essential prerequisite or condition precedent, like a special enabling act, in conferring the power and authority to make the proposed increase valid. Such approval involves the grant of power to complete and perfect the proceedings commenced by the association looking to an increase of its capital stock. It is something lying beyond the action or control of the association and its stockholders seeking to effect an organic and fundamental change in the constitution of the bank; and in respect to this essential thing, in nowise involved in the action or steps taken by the association, the question of irregularity or informality in its own mode of procedure, and the consequences thence resulting, do not apply."

Continuing on page 519, the Court takes up the case of Vedder vs. Mudgett, 95 N. Y., 295, and distinguishes between it and the case of Scoville vs. Thayer and approving the doctrine declared in the New York case, says:

"In Vedder vs. Mudgett, as the Court asserts, and as the statute shows, 'the abstract power did exist' on the part of the corporation to make the increase of its capital stock, and there was a way in which the increase could lawfully be made by the corporation's own action, independent of the sanction or approval of any state officials. The New

York statute under which the corporation acted was substantially like that of the Illinois statute under which the Upton cases, above referred to, arose, and which the Supreme Court held, conferred upon the corporation the power to make the increase of its stock, in the execution of which the irregularities and informalities occurred which were held, not to invalidate the stock. In the Vedder case, as in the Upton cases, there was color of compliance with the statutory requirements, which came within the power and legitimate action of the corporation. The want of conformity to the provisions of the law, relied on as rendering the stock void, were defects committed entirely by the corporation in respect to matters within its own control, and as to which it was invested with full authority."

Counsel for defendant in error, cannot find any case in which the question at bar is so well argued and presented as in this case from which we have quoted so largely, and we understand from the reasoning of the learned judge, that a failure on the part of the banking association to do those things which it had power to do under the act of Congress, and which was committed to it to do, to enable it to increase its capital stock, if it does also procure the necessary certificate from the Comptroller, does not relieve its shareholders who have taken part of the increased capital and received the full benefits of it, from having the doctrine of estoppel plead in its full force against them.

In the latter case, Stutz vs. Handley, 41 Fed. Rep. 531, the same learned judge fully discusses the difference betwen a lack of power on the part of the corporation and the mere non-performance of acts devolving upon itself or within its own control.

After quoting from the opinion of the Court in Scoville

vs. Thayer, Associate Justice Jackson on page 541 of case cited, says:

"The reason for the distinction thus indicated is founded upon the principle that a corporation has no inherent authority of its own motion, or by its own action, to effect fundamental changes in its constitution or organic law, such as an increase of its capital stock involves. It is an essential prerequisite or condition precedent to the validity of such a change that the sovereign by whom the corporation is created, or under whose law it is organized, shall give its consent thereto, either in the company's charter, or by some general or special act. But, when such authority is conferred, those who accept stock under the exercise of the power by the corporation are not allowed to *shield themselves from liability in respect thereto by setting up the failure on the part of the company or of themselves to perform any subsequent act or duty resting within its or their control, such as making, recording, or publishing a certificate of such corporate action.* This Court had occasion to consider and apply this distinction between lack of power on the part of the corporation and the mere non-performance of acts devolving upon itself or within its own control, in the case of Winters vs. Armstrong, 37 Fed. Rep., 508-520, where the subscribers for increased capital stock were relieved because the corporation failed and ceased to exist before it had acquired the requisite power to make the increase."

In the case of McFarland vs. First National Bank, 68 Fed. Rep. 868, the banking corporation never secured authority from the Comptroller of the Currency to increase its capital stock, and of course the final certificate declaring the increase and authorizing it to do business was never issued, and the Court simply held that although the shareholders had taken the preliminary steps to increase the

capital, yet the action of the Comptroller in refusing to issue a certificate prevented the increase from ever being made effective, or binding upon the subscribers.

It is no authority for the proposition contended for by the defendants.

Laredo Implement Co. vs. Stevenson, 66 Fed. Rep. 633, the United States Circuit Court of Appeals, held that the defendant, a subscriber to the capital stock of a corporation was not estopped to deny its validity by the fact that he had voted the stock when the corporation was absolutely without power to increase the stock, and in such case no act or consent of the shareholder who received such stock estopped him from denying its validity.

The want of power which will make the act of the corporation void so that no rights can be based upon them is very clearly defined in Citizens National Bank vs. Hawkins, 71 Fed. Rep. 370. The Court says:

"An act is *ultra vires* a corporation when it is beyond and outside of the scope of the powers conferred by its founders, when the corporation is without authority to perform it under any circumstances or for any purpose. Such acts are void and no contract for their performance can be enforced by or against the corporation, the plea of *ultra vires* being available to either party to the contract. There are, however, acts done in excess of conferred powers, illegal as to stockholders, but for which the corporation is liable to innocent third party. * * * In the case at hand no power is granted to purchase stock in another bank and therefore a prohibition to do so may be implied."

The Court continuing says, however, that the bank had a right to loan money on the shares of stock in another bank, and acquire the stock by a sale thereof under execu-

tion and that it therefore had a right under certain circumstances to acquire stock in a national bank, but it acquired the stock in question by purchase from a third party and had it transferred to itself. The acquisition was without the general scope of its powers.

"The case is, therefore, one of an abuse of a general power, a wrongful exercise of conferred power, for purposes and under circumstances contrary to law, and not in the exercise of a power not in any event given. It is therefore, related to the second class above noted to which the doctrine of *ultra vires* does not apply. In all such cases a corporation cannot set up its own violation of law to escape the responsibility resulting from its illegal act."

In Central Transportation Co. vs. Pullman Palace Car Co., 139 U. S., 24, where the same principle is discussed, it is held:

"A contract of a corporation which is *ultra vires* in the proper sense, that is to say, outside of the object of the creation as defined in the law of organization, and therefore, beyond the powers conferred upon it by the Legislature is not voidable only, but wholly void and of no legal effect. The objection to the contract is not merely that the corporation ought not to have made it, but that it could not make it. The contract cannot be ratified by either party, because it could not have been authorized by either. No performance on either side can give the unlawful contract any validity, or be the foundation of any action upon it. When a corporation is acting within the general scope of the powers conferred upon it by the Legislature, the corporation, as well as the persons contracting with it may be estopped to deny that it has complied with the legal formalities *which are prerequisites to its existence, or to its*

*action, because such requisites might in fact have been complied with.*"

In deciding the case of Vedder vs. Mudgett, 95 N. Y., 295, which has been referred to in the other cases cited, the Court on page 310, says:

"But no notice of such meeting of stockolders was given, as required by section 21, chapter 40, of the acts of 1848, nor was any certificate of the proceedings of such meeting made, or filed, as required by section 22 of the same act. The attempted increase was, therefore, illegal, but the respondent insists that, nevertheless, as against the creditors of the company, the defendant stockholders by accepting their proportions of the increased stock, by voting for its increase, by taking dividends upon it, and holding it out to those dealing with the company as an actual component of its capital, are estopped from denying the legal validity of the increase and must be held responsible as if it were valid. The authorities for this doctrine are numerous and strong. (Eaton vs. Aspinwall, 19 N. Y. 119; Chubb vs. Upton, 5 Otto. 665; Aspinwall vs. Sacchi, 57 N. Y. 331; B. & A. R. Co. vs. Cary, 26 id. 75; Kent vs. Quicksilver M. Co., 78th id. 159; Sheldon H. B. Co. vs. Eickemeyer Co., 90 id. 613.) The answer made to them is that an act absolutely and wholly void, because, under the law, incapable of being performed, cannot be valid by estoppel. This is true where under the law there is an entire lack of power to do the act which is brought in question. The distinction is well illustrated in Scoville vs. Thayer (105 U. S. 143). Under the law of Kansas no company like that then before the Court could increase its capital to more than double an amount originally authorized. The capital was sought to be increased in excess of that amount. As against creditors it was claimed to be a valid

increase by the operation of an estoppel, but the Court ruled otherwise, and justly; for the very foundation of estoppel, the misleading of creditors to their injury was wanting. The latter knew and were bound to know that no power existed to so increase the capital, and that, therefore, it was not increased; and hence they were not, and could not be misled. But whereas, in the present case, the power did exist, and there was a way in which the increase had been lawfully effected and the necessary steps had been taken, there the doctrine of estoppel may apply, and the increased stock be deemed valid as against the creditors who have acted upon the faith of such iscrease. The referee has found that each and every one of the present defendants have done some act which brings them within the range of the estoppel alleged, or hold shares of the stock which in the hands of the assignors stood charged and burdened with a liability for the company's debts. We must, therefore, treat the increase as lawful, and precisely as if the needed preliminary steps had in truth been taken."

The cases referred to—

*Upton vs. Tribblecock, 91 U. S. 45, and*

*Chubb vs. Upton, 95 U. S. 665.*

*Webster vs. Upton, 95 U. S. 65.*

*Sanger vs. Upton, 95, U. S. 56.*

All arose out of subscriptions to the capital stock of the Great Western Insurance Company, an Illinois corporation, are directly in point in the case at bar. The particular wording of the statute does not clearly appear from the decisions, but enough is apparent to show that no valid increase could be made under the statute except in compliance with its provisions.

The statement of the case in Chubb vs. Upton, 95 U. S. 665, is:

"In 1870, acting under the general laws of that state, (Illinois) authorizing insurance companies to increase their capital stock, the directors and shareholders of the company took measures to increase the capital stock and filed their papers for that purpose with the secretary of state and auditor of public accounts. By these proceedings the company undertook to increase its stock to $5,000,000. The company assuming that the stock had been increased, took subscriptions and issued certificates therefor and immediately commenced doing business, etc. (Page 665.)

Chubb subscribed for some of the stock and voted it at stockholders' meeting. When sued upon it for the unpaid part of his subscriptions, he offered to show in his defense certain alleged irregularities and informalities in the papers filed in public offices and to show that the holders of the stock in the original company never increased their stock or authorized anyone to increase it. (Page 666.) In the statement of the facts in this case as reported in the Lawyer's Co-operative Publishing Co., edition of these reports, book 24, page 523, it appears that the defendant offered to show that the original of the paper documents introduced on the part of the plaintiff, relative to increasing the stock of the company, were forged, etc."

All of this evidence was rejected. In passing on the questions presented, the Court, among other things, says:

"It is idle to deny that this was the case of an organization which claimed to have been taken and apparently supposed that it had taken, the measures required by law to complete the increase of capital. It acted as such and the defendant, by receiving his certificate of stock, entered into engagements with it as such. If it be conceded that

the increased stock was but *de facto* and that it could have been annulled or suppressed by the action of the attorney-general as acting under an irregular organi. zation, the defendant derives no aid from the admission. The cases cited are clear to the point that he cannot make the objections, but must perform the engagement he has made."

Then addressing itself to the more important question, that is, the offer to show that the holders of the stock never increased the capital nor athorized its increase, the Court says (Page 669):

"All this does not alter the fact that there was an attempted alteration of the company under the forms of law, approved by the attorney-general, with an increased capital, in the organization and management of which the defendant took part, that he paid his money, secured his certificate, of stock, attended meetings, voted, acted as an officer, and, so far as the records show, never repudiated his position at any time, even to the time of the trial. If successful, he would have shared in its profits. He may have been the dupe and victim of the action of others. He may have been an accomplice. At all events he was so far an actor in the affair that he cannot escape the consequences of his position."

This line of cases seem to us to fully answer the position taken by the counsel for plaintiff in error. They clearly hold that although the increase may not be valid, and could be successfully questioned by the shareholders at the proper time, or by the state by quo warranto, or other proceeding, yet the power is conferred to increase the stock in a certain way in certain event, and although it may not have been paid in, yet the defendant is estopped to show that fact by his action and he must stand by his engagement.

The cases growing out of the failure of the Pacific National Bank of Boston are fully in accord with the foregoing. That bank proposed to increase its capital stock $500,000 and the preliminary steps were taken, but when it was finished it was found that only $461,300 of stock had been subscribed and paid in. The directors had adopted a resolution to make the increase $500,000. The stockholders had a regular meeting called for the purpose, had voted to increase the capital stock $500,000, but subscriptions only to the amount of $461,300 were secured. Thereupon the board of directors certified that fact to the Comptroller and the Comptroller issued his certificate for an increase in the latter amount. Afterwards the bank failed and the subscribers to this increased stock were assessed 100 per cent. on the shares.

These cases are:

*Delano vs. Butler, 118 U. S. 649.*

*Aspinwall vs. Butler, 133 U. S. 595.*

*Pacific National Bank vs. Eaton, 141 U. S. 227.*

*Butler vs. Eaton, 141 U. S. 240.*

*Thayer vs. Butler, 141, 234.*

The liability upon the assessment made upon the increased shares seems to be put upon the ground that the matter about which objection was made was one wholly within the discretionary power of the corporation, subject to the approval of the Comptroller. Besides this the Court says it was not open to the subscriber to say what he did in receiving his shares was in ignorance of the facts, because opportunity and means of knowledge were such as by the exercise of common diligence he would have become acquainted with them and his course of action must be construed to constitute a complete acquiescence in and ratifica-

tion of, the previous action of the association and Comptroller of the Currency.

*Delano vs. Butler, 118 U. S., 652.*

They also fully answer the objection that the certificates for shares of the increased stock were issued before the Comptroller issued his certificate. In Pacific National Bank vs. Eaton, 141 U. S., 227, the Court quotes from the decision of the Supreme Court of Massachusetts from which the case came before them on error as follows:

"It will be observed that without waiting to see what the future action of the association and the Comptroller of the Currency might be on the question of the ultimate amount of the increased stock the plaintiff paid for his shares and accepted his certificate. This he did in legal contemplation with the knowledge of the law which authorized the association and the Comptroller to reduce the amount of the proposed increase to a less sum than that fixed in the original proposal of the directors, and such payment and acceptance of the certificates in accordance therewith might amount, under such circumstances, on his part to a waiver of the right to insist that he should not be bound, unless the whole amount of the proposed increase should be subscribed or paid in, but without insisting upon that point or deciding it, we think that the subsequent conduct of the plaintiff amounts to a ratification—118 U. S., 650. In the present case the plaintiff paid in his money but did not accept a certificate of stock."

The Court held the question fully settled by the previous cases of Delano vs. Butler and Aspinwall vs. Butler, and affirming what was said by the Massachusetts Court.

Many acts may be contrary to the provisions of the statute and so be held invalid and illegal as between the

shareholders and the corporation and yet valid in favor of creditors, or the act or contract may contravene the plain provision of the statute, and yet not be in legal contemplation void. The case of National Bank vs. Matthew, 98 U. S., 625, cites a number of such cases.

Mr. Morrawitz, in his work on corporations, section 839, says:

"When a person subscribes to the capital stock of a corporation he must be held to contemplate and intend that the corporation shall incur debts and pledge its capital, including the liability of its members for unpaid capital as security. Creditors who, in good faith, trust the corporation upon the faith of this security, stand in the position of innocent purchasers for value to the extent of their equitable lien; and it would be most unjust to permit a shareholder to disaffirm his contract and refuse to pay his share of the capital, for it has been thus pledged with his knowledge and consent to innocent third parties."

Congress could never have intended any such results to follow the use of the language used in prescribing the conditions and provisions in which national banking associations might increase their capital stock, and the Court will not put such a construction on the legislative intent as will do great injustice to those whom the law seeks always to protect, the innocent third party who contracts his debt on the faith of the capital of the association and the liability of its shareholders.

## III.

The plaintiff in error is not entitled, in this case, to a recision of his contract of subscription for many reasons:

*First.* He does not pray for a recision, nor state facts in his answer, which entitles him to one.

*Second.* He does not offer to return the 18 per cent. dividends, which he admits he received, nor to account for the same.

*Third.* His answer shows upon its face, that he was guilty of such laches, in discovering or attempting to discover that the bank had no real surplus, which could be declared into a dividend, as bars him from asserting that that fact, as a ground of recision.

*Fourth.* It is too late to rescind, after the insolvency of the bank, the appointment of a receiver, and the making of an assessment upon his stock, by the Comptroller of the Currency.

**First and Second.**

We need not further refer to the first and second reasons, *supra.* They will appear by a mere inspection of the answer. The legal effect of the failure of the plaintiff in error, to pray a recision, or to offer to return or account for the 18 per cent. dividends received, is elementary.

**Third.**

The attempt to excuse the laches of the defendtnt in not sooner discovering the fraud perpetrated upon them, by alleging that the books of the bank were so falsified by the bank that the real condition of the bank could not be discovered by the utmost diligence until after the failure of the bank, is no excuse at all, in law.

The subscription was made in 1890. The bank did not fail until May 4, 1894—three years and eight months afterwards. During this time they received eighteen per cent. of the par value of their stock in dividends. It is not pretended that they made any examination of the books

until after the failure of the bank and the appointment of a receiver.

This was not diligence, but laches, for it seems that they had no difficulty in discovering false entries as soon as the bank failed, and as stockholders, they had the right to examine the books of the bank at all times.

*Upton vs. Tribbilcock, 91 U. S. 45.*
*Sanger vs. Upton, 91 U. S. 64.*
*Ogilvie vs. Ins. Co., 22 How, 380.*
*Latimer vs. Bard, 76 Fed. page 541 and 542 and cases cited.*
*Chubb vs. Upton, 95 U. S. 667.*

Defendants admit that they received eighteen per cent of the par value of their stock in dividends. This they propose to keep, while asking to be relieved of liability on the assessment made upon the same stock upon which they received the dividends.

This they will not be permitted to do.

*Thomp. Liabil. Stockholders, 142.*
*Duffield vs. Iron Works, 64 Mich., 293.*
*Sanger vs. Upton, 91 U. S. 56 on 63 and 64.*
*Keyser vs. Heltz, 133 U. S. 138.*

And other cases *supra.*

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**Effect of Insolvency.**

The learned counsel for the plaintiff in error contend that it is not too late for a subscriber to the stock of a national bank to rescind his contract of subscription, after the bank has failed, the rights of creditors under the double liability clause accrued, and after a receiver has been appointed. In this case we differ with them, and think their position untenable.

There is much discussion in the authorities as to how long a subscriber to the capital stock of a corporation may stand quiescent and receive his dividends without any knowledge of any fraud in the organization of the company or increase of the capital, and after the discovery of the fraud, plead it as a defense. The rule so often invoked by parties who have been defrauded, that laches cannot be imputed to them until after the discovery of the fraud, does not apply to cases of this character.

The decisions heretofore cited from the Supreme Court of the United States and others clearly indicate this. In Chubb vs. Upton 95 U. S. 667, the Court declares that under such circumstances the subscriber must be vigilant in discovering the fraud and in repudiating it. The rule applies, as the Court says, in that case as well to the increase of the capital as to the original capital. In Upton vs. Tribbilcock, 91 U. S. 54, the Court says that the subscriber must be diligent in ascertaining the facts, his position and his liability in such case and prompt in repudiating his contract, and to the same effect is Sanger vs. Upton, 91 U. S. 63.

In Upton vs. Englehart, 3 Dillon 496, that learned judge discusses this question fully, and his opinion is cited with approval by the Supreme Court of the United States in the case to which we have referred.

If the subscriber delays discovering the fraud, or shows the want of exercise of the greatest vigilance in ascertaining the fraud imposed upon him, or the corporation, *until after its insolvency and the appointment of a receiver*, and when innocent third parties have contracted debts with the corporation, they will be held by their laches barred from setting up the fraud as any defense upon an assessment upon their stock.

This is pronounced to be the established doctrine in Cook on stockholders, Sec. 163 and by the Supreme Courts of Maryland and Michigan.

*Savage vs. Bartlett, 78 Maryland 561.*
*Bissel vs. Heath 98 Michigan 472.*
*Keyser vs. Heltz, 133 U. S. 138.*
Bailey vs. Sellinghost, 99 Fed. Rep. 801.
Langtry vs. Wallace, 97 Fed. 865.

In Duffield vs E. T. Barnum Wire and Iron Works, 64 Mich., 293, the doctrine of delay and estoppel is thus discussed by the Court:

"The rule that fraud vitiates all contracts, at the option of the person defrauded, applies as well to stock subscriptions in a corporation as to other contracts. Vreeland vs. New Jersey Stone Co., 29 N. J. Equity 188. Contracts induced by fraud are not void, but voidable, and the injured party has a right to have them abrogated. Relief can be had either at law or in equity, but will not be granted where the subscriber has been guilty of negligence in informing himself of the actual facts, or where, in consequence of his delay in repudiating the contract, *innocent third parties, either shareholders or creditors* have acquired rights which would be prejudiced by its recision. Thompson Liab. of stockholders 142. And it makes no difference in what aspect the question is raised, whether the subscriber who has paid for his stock repudiates the contract on the ground of fraud, and sues to recover it back, or the subscriber is sued for unpaid subscription, and defends on the ground of fraud. In either case, if the stock subscriber has been negligent in informing himself of the actual facts, *or if, in consequence of his apparent relation with the corporation as a stock subscriber, innocent third parties have acquired rights upon the faith of such relation*, which would be prejudiced by his

recision, he will be held as a subscriber, and will not be allowed, in the one case, to withdraw the capital which he has paid in, or, in the other, to escape payment." (Citing authorities.)

"The rule requiring the party defrauded to proceed with diligence to ascertain the truth or falsehood of such representations in order to entitle him to a recision of the contract, is well established in the Courts both of this country and England." (Citing authorities.)

"These decisions are based upon the ground that the *rights of creditors have intervened before the contract was repudiated*, and the insolvency of the corporation. To affect the right, there must be both creditors and insolvency or bankruptcy of the corparation before the right to rescind is exercised. In this case the right to rescind was not asserted or exercised *until after plaintiff knew of the insolvency of the corporation, and the rights of creditors*, who are represented by the receiver in this case, had intervened. It was then too late. Their rights are superior to his, because of his conduct and laches." (Citing authorities.)

In conclusion the defendant in error only desires further to call the attention of the Court to the fact that the plaintiff in error, as shown by the pleadings, subscribed for stock in this association, received the certificates, accepted dividends, and exercised all of the privileges and received all of the benefits as the holders of such stock for a period of nearly four years. They and their agents, the officers of said bank, had certified to the Comptroller of the Currency that the whole of the increased capital was fully paid in. Upon this representation he had issued to them the necessary authority to do business with the increased capital. They and their agents held themselves out to the community as having in all respects complied with the statute and

to have a full paid capital of $250,000. On the faith of this, men dealt with the bank, deposited their money with it, became its creditors, and years afterwards, after insolvency intervened, the plaintiff in error claimed to have discovered that the increased capital was not in fact paid in; pleading his own wrong, and the fraud and neglect of his own chosen agents. It is too late for this defense, and we think the judgment of the Circuit Court of Appeals, sustaining the motion of the defendant in error for judgment on the pleadings, should be affirmed by this Honorable Court.

All of which is respectfully submitted.

WM. S. SHIRK,

*Attorney for Defendant in Error.*

DEC 24 1900
JAMES H. McKENNEY
Clerk

Brf. of Sterry & Hagen for Plaintiffs

IN THE

# Supreme Court of the United States

**October Term, 1900.**

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| **C. HOOD,** *Plaintiff in Error,* *vs.* **T. B. WALLACE, as Receiver of the Missouri National Bank of Kansas City, in the State of Missouri.** *Defendant in Error.* | **TERM NO. 179.** (NO. 17,601.) |
| **C. J. LANTRY,** *Plaintiff in Error,* *vs.* **T. B. WALLACE, as Receiver of the Missouri National Bank of Kansas City, in the State of Missouri,** *Defendant in Error.* | **TERM NO. 180.** (NO. 17,602.) |

## BRIEF FOR PLAINTIFFS IN ERROR IN EACH OF THE ABOVE ENTITLED CASES.

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**By permission of the Court, this Brief is filed in No. 148. Particular attention is called to pages 27–43.**

IN THE

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## BRIEF FOR PLAINTIFFS IN ERROR IN EACH OF THE ABOVE ENTITLED CASES.

### STATEMENT OF FACTS IN EACH OF THE ABOVE CASES.

These cases were commenced in the United States Circuit Court for the District of Kansas by the defendant in error, as receiver, to recover the assessment ordered by the comptroller of the currency, against the shareholders of the Missouri National Bank, of Kansas City, Missouri, for an amount equal to $100 per share.

The petition in the case brought against C. Hood alleged him to be the owner of one hundred shares, the petition in the case against Lantry alleged him to be the owner of two hundred shares of the capital stock. In each case amended and supplemental answers, and cross-petitions were filed by the defendants. Each of these answers contained two separate and independent defenses, and also included a cross-petition to recover a judgment against the receiver for the amount paid to the bank for this stock; to each of these defenses and to each of the cross-petitions the receiver filed a general demurrer. These demurrers were, on hearing, severally sustained by the Circuit Court; no further amendments being made to the answers, judgment was finally rendered in the case against C. Hood, for the amount of the assessment claimed, to-wit: Ten Thousand Dollars ($10,000), with interest and costs, and in the case against the defendant C. J. Lantry, for the sum of Twenty Thousand Dollars ($20,000), with interest and costs.

Each of these cases were then taken upon a writ of error to the United States Circuit Court of Appeals, for the 8th circuit, and there, upon consideration, the judgment of the court below was affirmed in each case by a divided court. From these judgments of affirmance writs of error were taken to this court.

The facts stated in each of the two defenses and cross-petitions in each answer, to which the demurrers were sustained, are substantially as follows:

The Missouri National Bank of Kansas City, Missouri, was organized as a national bank in 1891, with a capital stock of $500,000, which apparently was all subscribed and paid for at the time of the organization. Early in July, 1893, this bank temporarily suspended payment. Upon its suspension the comptroller of the currency of the United States, after careful investigation into its affairs, determined that while the bank was in a sound financial condition, it should reduce its capital stock to $250,000, and that upon such reduction it would be permitted to continue its business as a national bank. The bank immediately reduced its capital stock

to the amount required by the comptroller, and on July 26, 1893, the comptroller issued two public bulletins as follows:

"This bank (referring to the Missouri National Bank of Kansas City) suspended on the 17th inst. because of a run on the part of its depositors. There was nothing in its condition to warrant this run or occasion suspicion as to its solvency. It seems to have been prudently managed and its resources are unusually free from items of questionable value, there being no bad debts. The bank is solvent and should be permitted to resume."

"The Missouri National Bank of Kansas City, Missouri, having complied with the conditions imposed by the Comptroller of the Currency, and its capital stock being unimpaired, has this day been permitted to reopen its doors for business. The bank opens with plenty of money on hand, and is wholly solvent and safe."

The bank continued in business at Kansas City from July 26, 1893, until December 3, 1896, when it was closed by order of the comptroller, and it and its business placed in the hands of the defendant in error, as receiver.

From the time of its original organization, until it was finally placed in the hands of the receiver, in December, 1896, the bank was absolutely insolvent, and in a wretched financial condition. Little or none of its capital stock (either as it was originally issued, or as it was left when it was reduced), was ever fully paid for, except, possibly, in some cases, by worthless and fictitious notes.

Prior to April 18th, 1896, of that year, the bank, through its president and cashier, sought to induce each of the plaintiffs in error (who were citizens of Kansas) to become connected with the bank, by the purchase of some of its capital stock. At the time of the negotiations with each of the plaintiffs in error, and at the time of the issuance of the certificates of stock to them, hereinafter set out, the bank was actually in a very bad condition, being utterly and hopelessly insolvent, on account of the lack of full payment in cash for its capital stock (all of which had been issued), bad loans, the withdrawal of money on fictitious notes and other paper, and on account of other reasons set forth in the answers. From the commencement of its organization up to late in the fall of 1896, the officers of the bank had so manipulated the books and assets of the

bank as to successfully conceal its actual insolvent condition from every one, including the comptroller and his examiners.

While the bank was in this condition the plaintiffs in error were induced to make an investigation into its affairs, by the false and fraudulent representations of its officers, with the view of becoming connected with it through the purchase of some of its capital stock; they made the most careful and searching investigation, as to the actual condition of the bank that it was possible for people situated as they were to make.

In this examination they found, not only the very favorable reports of the bank examiners, made from time to time, but also the certificates of character, and good standing, issued by the comptroller upon the re-opening of the bank on the 26th of July, 1893, as above set out. The plaintiffs in error employed to make this examination two expert bank examiners. These examiners were deceived, as had been the government examiners, and as finally were these plaintiffs in error, through the false and fraudulent representations of the president and cashier, and the false and fraudulent concealment of the facts, made by the manner in which the books were kept, and by the fictitious and forged bills receivable, and other fraudulent practices of these officers and others. At the very beginning of these negotiations, and from that time on, the president of the bank made to the plaintiffs in error, and to each of them, fraudulent and false representations, as to the condition of the bank, its resources and liabilities; representations that induced the plaintiffs in error, and each of them, to believe that the bank was perfectly solvent, and in the splendid condition that the comptroller believed it to be in when he issued to the public his bulletins above set out. The records of the bank at that time disclosed that the average daily deposits amounted to $1,500,000, and that its loans, in the shape of bills receivable, averaged about $1,300,000. While each of the plaintiffs in error believed and relied upon the false and fraudulent representations of the president and cashier, they left nothing undone, that was possible for men situated as they were

to do to fully acquaint themselves with the actual condition of the bank, before making the investment.

Prior to these negotiations certain stockholders of the bank induced the bank to purchase their stock from them, under threat to throw the stock they wished to sell on the market at such prices as would create exposure of the actual condition of the bank. The bank, under these threats, during the time referred to, attempted to purchase about 800 of its outstanding shares of capital stock, and paid to the stockholders holding the same the prices asked, either in cash belonging to the bank or by surrender of notes given by these stockholders in payment of the stock sought to be purchased, or by cash and by surrender of notes, as the case might be. Each of the persons engaged in these transactions knew that the bank was the real, actual attempted purchaser of the stock, and that its funds and its assets were being used in payment for the stock thus attempted to be purchased. In order to conceal the transaction from the knowledge of the government, and every one else the certificates for this capital stock held by the persons with whom these attempted purchases were made were either endorsed by such persons in blank or assigned to the name of some employe of the bank, and then delivered to the bank by the persons attempting to sell. The bank, upon receipt of the certificates, would substitute the worthless notes of insolvent employes of the bank for the cash paid, or assets used, by the bank in such attempted purchase. None of this stock, so attempted to be purchased, was taken, or purchased, or procured by the bank to prevent any loss or losses, upon any debt or debts previously contracted in good faith, or purchased in any way authorized by law, but was attempted to be purchased by the bank with its funds or assets for the sole purpose of preventing such stock from being sold in open market, and to prevent the owners of it from making an investigation into the actual condition of the bank. None of the parties in whose names the certificates for the capital stock attempted to be purchased was transferred ever paid anything for the stock, neither did they, or any of them, ever intend

to pay anything for the stock, or to pay any of the notes given to the bank to replace its funds used in the purchase of the stock, because it was agreed between them and the executive officers of the bank, that they should hold the stock in trust for the bank, and for its sole use and benefit. When the plaintiffs in error finally determined to purchase stock of the bank, they were informed by the president of it that the bank held some of its own stock, taken by the bank from debtors to prevent loss on debts previously contracted in good faith, and that the officers of the bank could purchase some more from friendly stockholders who were anxious to have plaintiffs in error become stockholders in the bank. Hood thereupon, about April 18, 1896, agreed to purchase one hundred shares of this stock from the bank at par value, to-wit: $100 per share, and Lantry agreed to purchase from the bank two hundred shares of the stock at par value of $100 per share, and Hood paid to the bank $10,000 in cash, and Lantry paid to the bank $20,000 in cash, and each received certificates for the number of shares of the capital stock alleged in the respective petitions filed in the court below by the receiver to be owned by them.

From the time the certificates of stock were issued to these plaintiffs in error up to the time the bank went into the hands of a receiver, nothing occurred in the management of the bank to arouse the suspicion of the plaintiffs in error, nor did they suspect anything until it was actually taken possession of by the receiver on December 3, 1896. At that time the books containing the history of the bank and the bank's affairs were turned over to the receiver, and *plaintiffs in error were severally denied access to them.* They made persistent efforts to secure all information possible about the bank's condition after the receiver was appointed, but were prevented from doing so by the receiver persistently refusing and denying such request (Transcript p. 10), sometimes giving as an excuse assurances that the bank was solvent and would pay its debts. Not satisfied with these refusals made to them by the receiver, they made appeals to the comptroller to permit them to investigate and

ascertain the actual condition of the bank, and permission was finally granted to them about the first day of September, 1897, to make such investigation. They at once procured the services of an expert bank examiner, who secured for them a history of the bank, as far as it could well be done. As soon as this report was made to them by their expert, *they became aware for the first time* of the frauds that had been perpetrated upon them, and that the bank had been hopelessly insolvent since its suspension in 1893, if not from the beginning.

Immediately upon learning this, they tendered their stock back to the receiver and demanded the return of their money. It will thus be seen that they had made the most careful and prudent investigation of the bank's affairs before they attempted to purchase any stock, and when it went into the hands of a receiver, made every effort in their power to ascertain its actual condition, and that, as soon as they became aware of the condition at the time of their purchase, they at once tendered the stock back and rescinded the contract of purchase. The character of the frauds finally discovered were not those such as occur between parties who deal with each other at arm's length, but were frauds that had been so adroitly concealed and covered up that they had escaped the detection for years of directors, stockholders, depositors, creditors—and even the vigilance of one of the ablest comptrollers of the currency that had ever occupied that office, together with his large force of expert bank examiners upon whom was conferred by law not only ample power to make full investigation, but the absolute duty of guardianship over banks like this one for the purpose of detection of such frauds. Not only did these frauds escape the detection of the comptroller's office, but that very office had placed a barrier in the way of their detection by certifying to the world that the bank was in a healthy and prosperous condition at a time when it was in truth rotten. After it went into the hands of a receiver, these frauds were not brought to light and made known to the world by the only person who was clothed with the power and charged with the

duty to do so, but it was left for these defendants to secure, after many efforts, permission from the comptroller's office to do so, and thereby learn for the first time that which should have been disclosed willingly by the receiver to every one interested.

On August 30, 1897, prior to obtaining permission to investigate, and while no one unless it was the comptroller, his receiver and the officers of the bank, were aware of the facts stated, the comptroller of the currency ordered an assessment of $100 per share against each shareholder. Each of the plaintiffs in error refused to pay this assessment, pending the investigation they were engaged in making, and were thereupon sued.

The answer setting out in detail the facts above stated is found on pages 5 to 16 of the record in case numbered 17,602 (term No. 180), and pages 5 to 16, in case numbered 17,601 (term No. 179).

There is in each case practically three main questions presented by the sustaining of the demurrers in the court below, and the affirmance of its ruling, by the Circuit Court of Appeals, which are as follows:

1st. Did the certificates issued by the bank to the plaintiffs in error make the plaintiffs in error shareholders of the bank liable to the assessment ordered?

2nd. Did these plaintiffs in error under the admitted facts have the right to rescind their contract of purchase of this stock at the time when they attempted to do so, and relieve themselves from the liability of the assessment ordered?

3rd. Had the plaintiffs in error the right to present their claims against the receiver, for the money paid to the bank at the time of their attempted purchase of this stock in a cross-petition filed in these causes of action commenced by the receiver to recover these assessments?

*Assignment of Errors in Case No. 17,601.*

(Title of cause omitted.)

1st. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in its ruling sustaining the demurrer of the plaintiff, T. B. Wallace, as receiver, to the first defense contained in the amended and substituted answer of defendant therein, C. Hood.

2nd. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in its ruling sustaining the demurrer of the plaintiff, T. B. Wallace, as such receiver, to the second defense stated and set forth in the amended and substituted answer of defendant therein, C. Hood.

3rd. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in favor of plaintiff, T. B. Wallace, as such receiver, against the defendant, C. Hood, upon the sustaining of said demurrer to the defenses contained in said amended and substituted answer of defendant, C. Hood.

4th. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in its ruling sustaining the demurrer of the plaintiff, T. B. Wallace, as such receiver, to the cross-petition in the answer in said cause contained.

Wherefore, the defendant, C. Hood, prays that the judgment of said court heretofore rendered against him be set aside and held for naught, and that he be restored to all things which he has lost by the rendition of such judgment.

*Assignment of Errors in Case No. 17,602.*

(Title of cause omitted.)

1st. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in its ruling sustaining the demurrer of the plaintiff, T. B. Wallace, as receiver, to the first defense contained in the amended and substituted answer of defendant therein, C. J. Lantry.

2nd. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in its ruling sustaining the demurrer of the plaintiff, T. B. Wallace, as such receiver, to the second defense stated and

set forth in the amended and substituted answer of defendant therein, C. J. Lantry.

3rd. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in favor of plaintiff, T. B. Wallace, as such receiver, against the defendant, C. J. Lantry, upon the sustaining of said demurrer to the defenses contained in said amended and substituted answer of defendant, C. J. Lantry.

4th. That the United States Circuit Court of Appeals erred in sustaining and affirming the judgment of the United States Circuit Court in its ruling sustaining the demurrer of the plaintiff, T. B. Wallace, as such receiver, to the cross-petition in the answer in said cause contained.

Wherefore, the defendant, C. J. Lantry, prays that the judgment of said court heretofore rendered against him be set aside and held for naught, and that he be restored to all things which he has lost by the rendition of such judgment.

# POINTS AND AUTHORITIES.

## FIRST POINT.

**The Circuit Court erred in sustaining the demurrer to the second defense in each answer, as the admitted facts in each of such defenses clearly established the proposition that neither one of the plaintiffs in error were shareholders of the Missouri National Bank, at the time of the levy of the assessments sought to be collected in these actions.**

I.

We briefly re-state the facts upon which this defense, in each case, is based:

The bank, having all of its capital stock outstanding, attempted, through its officers, to purchase 800 shares of such stock, from some of its shareholders, to prevent a threatened exposure, of its actual insolvent condition, by the parties holding such shares of stock. To carry out this scheme the officers of the bank took of its assets, a sufficient amount thereof, to pay for the purchase of these 800 shares to the holders thereof the prices agreed upon, and paying for the same, had the stock certificates, which had been issued therefor transferred, by the actual owners of these certificates and the stock represented by the same, either directly to the bank, or to some of its employes, to hold in trust for the bank. All parties to this transaction knew that the bank was using its assets to make this purchase, for the purpose stated, and for no other purpose, and that said purchase was being made for the bank. These transactions between the bank and its shareholders were bald, open violations of Section 5201 of the Revised Statutes of the United States, to the knowledge of all concerned. Upon receiving these certificates from its shareholders who owned them, the bank cancelled them, or a sufficient number of them, to enable it to deliver, without an apparent over-issue, a certificate to

plaintiff in error Hood for 100 shares, and a certificate to plaintiff in error Lantry for 200 shares (see printed Transcript, case No. 17,601, pages 12 to 15, and case No. 17,602, pages 12 to 15).

II.

That this attempted purchase of a portion of its own capital stock by the bank for the purpose admitted was *void* and not merely *voidable*, seems no longer to be an open question in this court, under the principles determined by it in the cases of:

California Bank v. Kennedy, 167, U. S., 362;

First National Bank of Concord v. Hawkins, 174 U. S., 364.

III.

The certificates, which were transferred to the bank, upon its attempted purchase of these 800 shares of stock, did not vest in the bank, either the possession of the stock, or the title to a single one of the shares, represented by such certificates. The certificates, *not being the stock itself*, but merely evidence of the ownership of the stock represented by them, could not, upon delivery to the bank, in direct violation of the provisions of the statute, divest the people transferring them, of their title to the stock, evidenced by such certificates.

Mr. Cook, in his work on Stock, Stockholders and Corporation Law (2nd ed.), paragraph 10, states the legal character of certificates of stock in corporations as follows:

"Certificate of Stock:—A certificate of stock is, from one point of view, a mere muniment of title, like a title deed. It is not the stock itself, but evidence of the ownership of the stock; that is to say, it is a written acknowledgment by the corporation of the interest of the shareholder in the corporate property and franchises; it operates to transfer nothing from the corporation to the shareholder, but merely affords to the latter evidence of his rights. It should be clearly apprehended that the certificate is not the stock, but merely written evidence of the ownership of shares. Accordingly, it follows that shares have no 'ear marks'—that one share cannot be distinguished from another share—but that it is only the certificates which are distinguishable one from the other by their numbers and in other ways. The certificate, therefore, has value in itself only as evidence, and apart from the shares

which it represents, it is utterly worthless. And even as evidence, it is not in every case essential; it is merely a convenient voucher, which the shareholder has a right to receive if he asks for it. One element of its value to the shareholder is that it is prima facie evidence of his title."

Judge Thompson, in his recent work on Corporations, volume 2, section 2348, states the proposition as follows:

(The italics are ours.)

"And, first, it is to be observed that such a certificate is merely the paper representative of an incorporeal right, and that it stands on a similar footing to that of other muniments of title. It is not in itself *property*, but is merely the *symbol* or paper evidence of property. Hence, the proprietary right may exist without the certificate. Numerous cases accordingly hold that a person may acquire the rights and incur the liabilities of a shareholder, both to the corporation and to its creditors, although no certificate has, in fact been issued. Corporate shares have also been classed as 'securities.' And although they may be thus designated within the meaning of particular statutes, yet it is plain that they are not securities in the proper sense of the word. 'Certificates of stock are not securities for money in any sense; much less are they negotiable securities. They are simply the muniments and evidence of the holder's title to a given share in the property and franchises of the corporation in which he is a member.' The following further observations in the same line of thought were made by Mr. Justice Crockett: 'If a firm doing business as an ordinary partnership issue certificates to each of its members specifying the interests of the respective copartners, such certificates would have no intrinsic value, except as evidence of the *quantum* of interest of each copartner. The joint interest of the copartner in the property and business of the firm is the substance of the existence of which the certificate is but the evidence. If, for example, there be three copartners, each owning an undivided interest of one-third, there is no appreciable difference between the respective interests. They are in all respects precisely similar, and each several interest is an exact duplicate of the others. The same principle is applicable to corporations. The holder of ten shares of stock stands precisely upon the same footing as any other holder of ten shares. Their interests are precisely similar and of the same value, and each holds but an undivided interest in the common property.' From the principle that the certificate is not the property itself, but merely the muniment of title, it has been held that the duties, privileges and responsibilities of the holder of it cannot be divested by the mere act of writing across the face of it the word 'cancelled,' and returning it to the secretary of the com-

pany. As a certificate is not necessary to make one a shareholder, *so the surrender of it to the company does not necessarily make the holder of it cease to be a shareholder.*"

See also:

Telegraph Co. v. Davenport, 97 U. S., 369;

St. Romes v. Levee Cotton Press Co., 127 U. S., 614;

Hammond & Co. v. Hastings, 134 U. S., 401;

Johnson v. Laflin, 103 U. S., 800;

National Bank v. Watsontown Bank, 105 U. S., 223.

The case of Burrows v. Niblack, decided by the Circuit Court of Appeals of the 7th circuit (84 Fed. 111), is precisely in point. This case was an action brought by the receiver of the Chemical National Bank of Chicago, to recover from Burrows $10,000 paid to him, by that bank for a hundred shares of its own outstanding capital stock, attempted to be purchased from Burrows, while it was a going concern. We quote from the opinion in this case, illustrative of the point in question, as follows:

(The italics are ours.)

"The principal objections urged are: (1) That the validity of the purchase by the bank of its own stock can be questioned only by the government; (2) That the alleged liability of the bank for the return of the money can be enforced only in a court of equity; and, (3) That a tender back of the shares of stock purchased, was essential to the right of recovery of the price paid. The first objection is based upon that line of decisions of which illustrations are found in Bank v. Matthews, 98 U. S., 621; Bank v. Whitney, 103 U. S., 99; and Thompson v. Bank, 146 U. S., 240, 13 Sup. Ct., 66; but the present case, as we think, is governed rather by the principles declared in McCormick v. Bank, 165 U. S., 538; 17 Sup. Ct., 433; and Bank v. Kennedy, 167 U. S., 362; 17 Sup. Ct., 831, where the line of cases mentioned is distinguished. The transaction here in question was not a purchase made for the purpose of preventing, or which was necessary to prevent, loss upon a debt previously contracted, but as set forth, it was a bald purchase by the bank of its own stock for cash, and necessarily involved for the time being a reduction *pro tanto* of the corporat- stock. Even if it were not forbidden by the statute, the transaction would be inconsistent with public policy and with established principles of law. The suggestion that a reduction of stock by a national bank may be lawfully made under section 5143 of the revised statutes is irrelevant because it is not shown, and

without proof is not to be presumed, even if it were conceivably possible, that this transaction could have been justified under the provisions of that section. The purchase was outside of and beyond the powers of the bank, and therefore, as a corporate act, was void from the beginning; and, while it appears from the agreement that the certificates of stock were endorsed in blank and delivered to the president of the bank, *the latter did not thereby acquire, nor the plaintiff in error part with, title to the stock.* The money having been unlawfully paid out, the bank had an immediate right of action to recover it in an action of assumpsit. *It was not necessary to go into equity nor to offer a return of stock.*"

This Court has practically held that in such case it is not necessary to make any tender or demand.

Pence v. Langdon, 99 U. S. 578.

IV.

The shareholders, from whom these 800 shares of the bank's capital stock, was attempted to be purchased by the bank, remained, after the transfer of the certificates to the bank, or its employes, just as much, the owners of the stock, attempted to be transferred, as they were prior to such attempted transfer. They were the persons, whom the receiver, should have called upon to pay these assessments, instead of calling upon the plaintiffs in error. It has been constantly held, by the Federal Courts (including this court) that the real owner, of the shares of capital stock, of an insolvent corporation, is the party who should be held liable, for assessment, where an assessment of stockholders for the benefit of creditors is authorized.

Pauly v. State Loan and Trust Co., 165 U. S. 606, and cases therein cited;

Stuart v. Hayden, 169 U. S., 1;

Lucas v. Coe, 86 Fed. 972.

V.

The certificates issued to Hood and Lantry, purporting to convey one, and two hundred, shares of its capital stock, were each for an actual over-issue of stock, and hence did not, make either Hood, or Lantry, a shareholder in this bank. In support of this

proposition, we quote from the text of Cook on Stockholders, etc. (4th Ed., Par. 292).

"By over-issued stock is to be understood stock issued in excess of the amount limited and prescribed by the act of incorporation. Certificates of stock issued in excess of the certificates that represent the full authorized capital stock of the corporation represents over-issued stock. Such stock is spurious and wholly void. This is the settled law, and it prevails equally whether the over-issue is the result of accident or mistake, or want of knowledge of the law, or is due to fraud and intentional wrong-doing. The *animus* or intent of the parties to the over-issue is not material. Over-issued stock, no matter how over-issued, represents nothing, and is wholly and entirely valueless and void. So rigid and well established is this rule that not even a *bona fide* holder of such stock can give to it any validity or vitality."

The leading case upon this subject is that of New York, etc., R. R. Co. v. Schuyler, 34 N. Y., 30.

If these certificates, represented nothing but over-issued stock, under the decision of this court, (Scovill v. Thayer, 105 U. S., 143), neither Hood, or Lantry, acquired any rights as stockholders in this bank, or assumed any liability, for the assessments in controversy.

See also the decision of the United States Circuit Court of Appeals, eighth circuit, in the case of Laredo Improvement Co. et al. v. Stevenson (66 Fed., 633); and the following cases:

Kampmann v. Tarver (S. C. of Tex.), 29 S. W., 768;

Kellerman v. Maier, et al., 116 Cal., 416;

Christenson v. Eno, 106 N. Y., 97;

Andrews et al., v. National Foundry & Pipe Works, 22 U. S., C. C. A. Rep., 110;

Gillman v. Gross (S. C., Wis.), 72 N. W. R., 885;

Tschumi v. Hills (C. A., Kas.), 51 Pac. 619;

Follett v. Stevens et al., 43 Fed. Rep., 842.

In view of the above decisions, it seems to us that the reasoning of the court below upon this proposition was unsound (printed transcript, pages 29 to 39). The court below admits, that the transaction between the bank, and its shareholders, in the at-

tempted purchase of this stock, was *ultra vires*, but then proceeds to argue, that because the bank fraudulently took the money, of plaintiffs in error, and thereby restored its impaired assets, to that extent, the plaintiffs in error, were in no position, to take advantage of this transaction, for the purpose of relieving themselves, of the liability to an assessment. In other words, the court held: That the law imposed upon each of the plaintiffs in error, a penalty, for the sole reason, that the bank, had been able to defraud each of them, in a case, where neither of the plaintiffs in error, were guilty of any laches, holding further that, this penalty, was imposed for the sole benefit of persons who would have received precisely the same benefit, if the assessment had been levied against the real owners of the stock, who had attempted fraudulently to rid themselves of such a burden.

The court also held that only the government had the right to inquire into such transactions, although the transactions were prohibited both by the statute, and by public policy, overlooking the principles, determined by this court in the recent decisions in McCormick v. Market Nat. Bank (165 U. S., 538); California National Bank v. Kennedy, *supra;* First National Bank of Concord v. Hawkins, *supra.*

The majority of the court below, also overlooked the fact, that the transfer of the certificates, to the bank, was not the transfer of the stock itself, and overlooking this, assumed that the shares of stock, attempted to be sold to the bank, were themselves, in some way, transferred to the bank, and by the bank transferred to each of the plaintiffs in error. This will be seen by reading the opinion of Justice Thayer, from which we quote the following paragraph:

"The creditors of the bank who must be presumed to have extended credit on the security afforded by the capital stock and the statutory liability incident thereto, cannot be deprived of such security, either by the fact that the defendant was fraudulently induced to become a shareholder or by the further fact that the bank had wrongfully acquired the stock which it subsequently sold to him, when it appears that he knowingly became a registered shareholder and remained such for eight months and until insol-

vency supervened and in the meantime enjoyed all the rights and privileges incident to that relation."

That this position of the court is untenable, must, upon consideration be apparent. All will concede, that if the capital stock was all outstanding, at the time of the issuance of the certificates to the plaintiffs in error, that such certificates only represented over-issued stock, and under the decisions of this court (in Scoville v. Thayer, and other cases cited), and would be absolutely void. The fact that Hood and Lantry for eight months severally acted as shareholders on the faith of such certificates being valid gave no validity to such certificates.

Can it be possible, that because of the fact, that prior to the issue of the two certificates, to the plaintiffs in error, the bank had attempted to purchase 800 shares of its capital stock, and had cancelled the certificates therefor assigned to it to the amount of the shares, attempted to be transferred to plaintiffs in error, that the certificates in question, were of any more validity, than they would have been, if at the time of their issuance, the bank had not made these attempted purchases, and all of its capital stock appeared to be (as it actually was) outstanding, upon the books of the bank.

If the position of the court below be correct, that the bank got actual possession of these 800 shares of capital stock as tangible things, through its transaction, and actually sold, and delivered 300 of these 800 shares to the plaintiffs in error, it would not follow that the plaintiffs in error, became shareholders, because it must be conceded, that the bank never got any title to any one, of these 800 shares; that neither it, or its receiver, would, under the decisions of this court, be estopped to say in any litigation whatever, that it did not acquire the title to a single share of this total of 800 shares.

Hence it follows that plaintiffs in error, by their purchase from the bank, got nothing, and should be no more estopped to say, that they did not acquire anything, than their assignor, or its receiver, would be estopped to say, the same thing, if upon a distribution of assets by the receiver, after paying the debts, the

plaintiffs in error claimed some part thereof as shareholders. If the receiver, had sued some of the shareholders, who transferred their certificates to the bank, to recover from them the assessment made against such transferred stock, could such shareholders have successfully defended, upon the ground, that although the transaction, between them, and the bank, was void, yet the bank was not injured thereby, having sold to the plaintiffs in error, the same shares of stock and that the plaintiffs in error, were the ones liable to such assessment, instead of themselves? We think it surely must be the law, that the receiver, could recover a judgment against any one or all of the parties, who attempted to transfer this stock, for the assessment of the stock attempted to be transferred. If this view be correct, would any court hold, that the plaintiffs in error would also be liable, for an assessment upon the same stock? No creditor has the right to ask for an assessment of any number of shares, of the capital stock, of an insolvent national bank, beyond the number actually authorized to be issued, or which may have been issued through some attempted compliance with an authorization therefor.

VII.

That the doctrine of estoppel as applied by the court, below, has no application, to one holding over-issued shares of stock, is, as it seems to us, thoroughly settled by the decisions of this court in Scovill v. Thayer, Bank v. Kennedy and Bank v. Hawkins, *supra*.

We had supposed that this point was thoroughly settled by the court below, in a decision rendered by it on March 4, 1895, in the case of Laredo Imp. Co. et al. v. Stevenson (66 Fed. 663), until it rendered its decision in the case at bar. We quote from the opinion in that case as follows:

"Is the defendant estopped by the fact that he once voted his stock, and that the officers of the corporation represented that its capital had been increased to $1,200,000, from asserting, against the creditors of the corporation, that the stock issued to him was void? This question must be answered in the negative. Where a corporation has power to issue stock or to increase its capital stock,

and this power is defectively or informally exercised, the acts and acquiescence of the stockholder may estop him from denying the validity of the stock or his liability therefor. Upton v. Tribilcock, 91 U. S. 45; Chubb v. Upton, 95 U. S. 665; Pullman v. Upton, 96 U. S. 328; Hadley v. Stutz, 139 U. S. 417, 425, 11 Sup. Ct. 530; Veeder v. Mudgett, 95 N. Y., 295, 310. But where the corporation is absolutely without power to issue the stock, or to increase the capital stock above a certain limit, no act or consent of the stockholder who receives stock issued without authority can estop him from denying the validity of the stock, or his liability therefor. The holder of such stock is under no obligation to pay for it, because he has received no consideration for such an obligation. The stock issued to him is absolutely void. He is not estopped to deny its validity, as against a creditor of the corporation, for the foundation of estoppel is deceit, and the creditor cannot be deceived as to the power of a corporation to issue such stock. He is bound to examine and know the law which limits the powers of the corporation with which he deals, and, whether he examines it or not, he is charged by the law with the knowledge of it. Scovill v. Thayer, 105 U. S. 143, 149; American Tube Works v. Boston Mach. Co., 139 Mass., 5, 29 N. E. 63; Reed v. Machine Co., 141 Mass. 454, 5 N. E., 852; Lathrop v. Kneeland, 46 Barb., 432; Merrill v. Gamble, 46 Iowa, 615; Merrill v. Reaver, 50 Iowa, 404; Clark v. Turner, 73 Ga., 1; Lincoln v. Express Co. (La.) 12 South, 937."

See also to same point:

Chemical Natl. Bank of New York v. Cal. Natl. Bank, 120 Cal., 601;

Kellerman v. Maier, et al., 116 Cal., 416;

Christenson v. Eno, 106 N. Y., 97;

Andrews, et al., v. Natl. Foundry & Pipe Works, 22 U. S. C. C. A., 110;

Gillman v. Gross, (Wis.) 72 N. W., 885.

Kampmann v. Tarver (Tex. S. C.), 29 S. W. R., 768;

Winters v. Armstrong, 37 Fed. 509.

Hayden v. Charter Oak Driving Park, 63 Conn. 142;

Page v. Austin, 10 Can. Sup. Ct. 132;

Clark v. Turna, 73 Ga. 1;

Insurance Co. v. Kamper, 73 Ala., 325;

Veeder v. Mudgett, 95 N. Y., 295;

Mallory, et al. v. Hananer Oil Works (S. C. Tenn.), 8 S. W. Rep. 396.

## SECOND POINT.

**The court below erred in sustaining the ruling of the Circuit Court upon the demurrer to the first defense in each answer.**

### FIRST.

The appointment of a receiver for this bank, and the making of the assessment ordered by the comptroller, did not limit or destroy, the right of either of the plaintiffs in error, to disaffirm their contract, with the bank, for the purchase of the shares of stock, from the bank, under the admitted facts stated in each of the defenses.

I.

Preliminary to the discussion of the proposition stated we recall the court's attention to the following facts, to wit:

The plaintiffs in error, at the time when these actions were brought, were still in utter ignorance of the actual condition of the Missouri National Bank of Kansas City. While at that time they had the right to assume that each of them had been induced to purchase this stock from the bank through fraudulent representations made by it, owing to its then inexplainable insolvency, yet the receiver, by his persistent refusal to permit them to investigate the books and other records of the bank, prevented their ascertainment of the actual facts in the case, which possibly would make a defense upon that ground. Subsequently, in September, when they finally obtained permission from the comptroller to make an investigation, the first find they made in such investigation, was the fact of the utter insolvency of the bank, from the time it commenced business, until the time its doors were finally closed; such fact at once disclosed, for the first time, to them, that the representations made to induce the purchase of stock were false and fraudulent, and entitled them to rescind their contract of purchase, which they at once did, and then plead the facts concerning the fraud and their rescission, in their answers, before the subsequent discovery, that the bank had no stock to sell. Subsequently, after the filing of

the first answers, setting out these defenses, the further investigation by their experts into the affairs of the bank revealed the fact that the bank did not own any stock at the time of its attempted sale of three hundred shares to them. Upon the ascertainment of this further fact, the present answer was filed, containing each of these defenses, as additional to those already filed. These parties, and their counsel, yet feel that, under the uncertainties of the situation, induced by the fraudulent system of keeping the books, and accounts, of the bank, each of these defenses should be maintained, to meet any possible proof, that may be made by the receiver. While each one of these defenses is distinctive from the other, each one is to some extent, interwoven with the other. The first defense sets out at length the sale to the plaintiff in error, Hood, of one hundred shares of stock, and to the plaintiff in error, Lantry, of two hundred shares of the capital stock of this bank, by the bank, under such fraudulent representations as would, without question, so far as the bank was concerned, entitle Hood, and Lantry, to severally rescind the contracts of purchase, and recover from the bank the price paid, at the time when the rescission was made.

These sales were made April 18, 1896, and the bank was put in charge of the receiver December 3, 1896. The receiver, upon taking charge of the bank, entered into and retained possession of all of its property, including the rooms and furniture, where it did business, and the executive officers of the bank, left the state of Missouri, prior to the discovery of the fraud, by the plaintiffs in error.

Plaintiffs in error, upon ascertaining the fraud practiced *at once* tendered to the receiver the certificates of stock, which had been issued to them, and demanded of him the repayment of the money paid by them to the bank for such stock. The receiver was at that time in sole possession of the bank, its rooms, and its assets, and he was the only one who could allow, at that time, these claims as claims entitled to participate in the distribution of such assets as he might thereafter distribute to creditors.

II.

Under the Kansas Code of Civil Procedure as construed by the Supreme Court of that state, the rule of the common law, with reference to the construction of pleadings demurred to, does not obtain; but on the contrary the rule in force in that jurisdiction, is, that not only every fact stated, or attempted to be stated, (however defectively) in pleadings, must, as against a demurrer, be construed, not only most favorably to the pleader, but only those presumptions, which are in favor of the pleader, (arising from the facts plead,) can be considered by the court in construing such pleadings.

Stewart v. Balderson, 10 Kas., 148;
Crowther v. Elliott, 7 Kas., 235;
Stringfellow v. Alderson, 12 Kas., 112;
McPherson v. Kingsbaker, 22 Kas., 646;
State v. School District, 34 Kas., 241;
Street Railway Co. v. Stone, 54 Kas., 83.

Section 914 of the Revised Statutes of the United States, requires the adoption of this rule, by the Circuit Court, of the United States, for that district, in all common law cases, where it would be applicable.

Glenn v. Sumner, 132 U. S., 152;
Roberts v. Lewis, 144 U. S., 653;
Central Transportation Co. v. Pullman's Palace Car Co., 139 U. S., 24.

Construing the allegations, in each of these defenses, against the general demurrers, filed to them, under either the rule of the common law, or the Kansas rule, it would be difficult to conceive of a more startling case of fraud, than that, which was perpetrated, upon each of the plaintiffs in error, by the bank itself, and which fraud admittedly, induced their several purchase of the 200 and 100 shares of its capital stock.

It will be admitted by all that the discovery of this fraud, at any time prior, to the appointment of the receiver, would have

given to each of the plaintiffs in error, the instant right, to rescind their several contracts of purchase, regardless of any question of solvency, or insolvency, of the bank at the time of the rescission.

Smith v. Reese River Mining Co., Law Reps., 2 E. Q. 264;
Venezuela Co. v. Kisch, Law Rep. 2 H. L., 99;
In re Brinsmead & Sons, 67 Law J., Ch. 11, 1 Ch. 104. 77 Law, 7 (N. S. 521);
Motor Co. v. Parnell, 75 Md., 113;
Tyler v. Savage, 143 U. S., 79;
Barnes et al., v. Gates (C. C. A., 4th Ct.), 89 Fed., 783.

II.

The right of one, who by fraud, has been induced to purchase, from a national bank, shares of its capital stock, to rescind such purchase, and thereby release himself, from the liability imposed by the statute, is based upon the proposition, that the liability of a shareholder, in a national bank, under the provisions of Section 5151 R. S., is, in most cases, voluntarily assumed, by the contract of purchase, and, therefore, in such cases, contractual in its nature, standing or falling, with the contract creating it. The failure on the part of the court below, to recognize this proposition is, we believe, the chief cause, for the decision complained of. The question whether this liability, under the provisions of similar statutes in various states, is a contractual one, or not, has been determined several times, by this court, and notably by it in its recent decision, in Whitman v. National Bank of Oxford (176 U. S., 559), where many of the authorities, are reviewed.

See also:

Hawthorn v. Calef, 2d Wall, 10;
Flash et al. v. Conn, 109 U. S. 371;
Richmond et al. v. Irons et al., 121 U. S., 27;
Stewart v. Hayden, 169 U. S., 1.

While every person, who becomes a creditor, of a national bank, has the right, to rely upon the fact, that if the bank, should become insolvent, while he remains a creditor, its registered share-

holders, would *prima facie* be liable to an assessment, equal to the amount, of the outstanding capital stock, held by them, yet one giving credit, to a national bank, has no right to rely upon the fact, *that any one individual shareholder, will remain such shareholder* (subject to the liability of the statute) *for any period of time*, however much such person's connection with the bank may have influenced the credit given; neither has such a person the right to *conclusively* presume that the names of those appearing on the list, of registered shareholders, upon the insolvency of a national bank, are all rightfully there.

Whitney v. Butler, 118 U. S., 655;

Stuart v. Hayden, *supra.*

Every creditor, or proposed creditor, of a national bank, is charged with the knowledge, that every shareholder, of such bank, can cease to be a shareholder, and relieve himself, from the liability, assumed by the ownership of some of its shares, at any time, either by the transfer in good faith, on the registry of the bank, of his shares of stock, to some one else, or by rescission of the contract, which created him a shareholder, when the right of rescission exists. To presume, therefore, (as did the court below) from the facts stated in each of these defenses, that during the connection of the plaintiffs in error, with the bank, their names obtained for it credit, it otherwise, would not have had, not only ignores the Kansas rule referred to, concerning presumptions arising from pleadings demurred to, but adds no argument against the right of each of the plaintiffs in error to rescind the contract at the point of time each did rescind. This several right on their part, to rescind their several contracts of purchase was created by the principles of the common law, and not by force of any statute. There being no statute giving the right to rescind, under facts such as are stated in these defenses, or under any state of facts for that matter, or fixing the time, within which such rescission should be made, the time, of the exercise of such right, is only limited, and controlled, by the requirements of the common law which created it. The only limitation imposed by the common law, as to the time,

when the right of rescission must be exercised, in this class of cases, is, that it must be exercised, within a promptly reasonable time after discovery, (by the party injured), of the fraud creating such right. The proposition above stated, is well illustrated, in the analogous cases of insolvency, where there has been an assignment, or a receiver appointed, and is also illustrated, by the decisions, under most bankruptcy laws. In such cases, it has generally, (if not universally) been held, that the assignment, or the appointment of a receiver, in no way affects rights, which could be asserted against an assignor, or bankrupt, if no assignment had been made, or receiver appointed. This is well illustrated, by the following decisions of this court, each of which, seems to us, very applicable:

Donaldson, assignee, v. Farwell, et al., 93 U. S., 631;
Yeatman v. Savings Institution, 95 U. S., 766;
Stewart v. Platt, 101 U. S., 738;
Porter v. Lazea, 109 U. S., 84.

Guided by the common law, (there being no statute), this, and other courts, have frequently held, that a receiver, of a national bank, upon his appointment, takes *all* of the assets of the bank, (including the shareholders' liability), in trust, for the creditors, and the stockholders, *subject to all claims, and defenses, that might have been interposed, against the insolvent corporation itself, with respect to any of such assets.*

Scott v. Armstrong, 146 U. S., 499;
Whitney, et al., v. Butler, 118 U. S., 655;
Briggs v. Spaulding, 141 U. S., 132;
Finn v. Brown, 142 U. S., 56;
Winters v. Armstrong, 37 Fed., 509;
Cutting, Receiver, v. Damerel, 88 N. Y. 411;
Hayes v. Shoemaker, 39 Fed., 319;
Young v. McKay, 50 Fed., 394;
Snyder v. Foster, 73 Fed., 136.

As stated by this court in the head-notes to the case of Scott v. Armstrong, *supra*:

"The receiver in such case takes the assets in trust for the creditors, and, in the absence of a statute to the contrary, subject to all claims and defenses that might have been interposed against the insolvent corporation."

See also:

Fourth Street Bank v. Yardley, 165 U. S., 653;

Yardley v. Philler, 167 U. S. 360.

The proposition as stated in Winters v. Armstrong, (37 Fed. 508) in reference to the question here discussed by the late Justice Jackson is as follows:

"The receiver stands in the shoes of the bank and can assert no rights against the subscribers which the bank could not have asserted."

One of the most important assets, that is vested in a receiver of a national bank, is the liability of the shareholders, of such bank, to respond, to an amount equal, to the face value of the shares of capital stock, held by them. It is hard to perceive upon what theory a shareholder, might prevent the enforcement of any other liability by a receiver of a bank growing out of a contract made with the bank while it was a going concern, on the ground that such contract, was induced by the fraud of the bank, and yet not have the right, to make the same defense, against his liability as a stockholder, in a case, where he was induced to become a shareholder, through a contract with the bank procured by fraud, and in a case where he has not been guilty of laches, in not discovering the fraud, prior to the appointment of a receiver.

III.

Following the principles established by the authorities above cited, it has generally been held, in the United States, where the question has arisen, that the assignment of, or the appointment of a receiver, for a corporation, on account of insolvency, does not, of itself, cut off from a stockholder in such corporation, his right to rescind his contract of subscription, or purchase of stock, induced by the fraud of the corporation if he has not been guilty of laches, in asserting such right.

In the eighth circuit, until quite recently, this proposition was considered to be the settled law, of the federal courts, in that circuit, as will be seen, by reference to the following cases:

Upton v. Englehart, 3 Dill. 496, was a suit brought by the assignee of an incorporated company to recover on the stockholders' liability; the defendant pleaded that he was induced to purchase the stock by the fraudulent representations of the agent of the company, and that he was in no way bound thereby, and that he not long ago repudiated said purchase by refusing to pay any more of the installments. Judge Dillon held the plea to be defective, because it did not show that the defendant made use of reasonable diligence to make himself acquainted with the matters in respect of which the fraud is claimed, nor when or how he repudiated the contract. And after referring to Oakes v. Turquand, and other English cases in which it had been held that the defrauded shareholder must make application to have his name removed from the register of shareholders before winding up proceedings are instituted against the company, the learned judge says:

"These decisions are doubtless, in some degree, influenced by the special provisions of the English corporations act, of 1862; but the general course of reasoning therein is applicable to cases of insolvent or bankrupt corporations in this country. There is no register of stockholders in Illinois, and it is possible that the decisions in England requiring active steps by bill in chancery to have one's name removed from the register might not be applicable in their full extent here. Indeed, I am inclined to the opinion that if a company has fraudulently represented or concealed material facts, and thus drawn an innocent person into the purchase of stock, he at the time being guilty of no want of reasonable caution and judgment, and afterwards guilty of no laches in discovering the fraud, and he thereupon repudiates the contract and offers to rescind the purchase—these facts concurring, I am inclined to the opinion that the bankruptcy of the company, subsequently happening, will not enable the assignee to insist that the purchase of stock is binding upon him."

The late Justice Miller also held precisely the same doctrine in the case of Farrar v. Walker (3 Dill. 506).

We call special attention to the two decisions of the court below

in Newbegin v. Newton National Bank, et al. (one reported in 14 U. S. C. C. A., 71, and the other in 20 U. S. C. C. A., 339). The syllabus in the first decision in the case reads as follows:

"One induced to subscribe for certificates alleged to represent an increase of the capital stock of a national bank at a time when no increase had been authorized, upon false representations of the cashier as to the bank's condition and ability to pay dividends, it being, in fact, insolvent at the time, is entitled to a judgment against the bank and its receiver for the purchase money paid.

"In an action against a national bank and its receiver to recover money paid under false representations as a subscriber for an increase of capital stock, a jury being waived, the court found facts clearly entitling plaintiff to recover. It then further found that the certificates of stock were issued on July 22, 1890; that the bank had no authority to issue such certificates; that the increase of stock was not authorized until the twenty-fourth day of September, 1890; that plaintiff was guilty of laches in not returning said certificates and demanding his money until after the bank had passed into the hands of a receiver, and in not bringing his action to recover said money sooner. The court thereupon rendered judgment for defendants. *Held*, that there was nothing in the finding sufficient to support the conclusion as to laches, and that the judgment must be reversed."

The case was again tried in the lower court and the plaintiff recovered a verdict and judgment and the case was again appealed to the court below. In the meantime the Newton National Bank had been reorganized and in fact, made the defense, depending mainly upon the proposition that the rescission or disaffirmance, on the part of the plaintiff was not made sufficiently prompt, and that the insolvency and appointment of a receiver barred the right to make it at all. A very able and interesting opinion was delivered by Justice Thayer, which we quote at length from, as follows:

"A more important question to be next considered, is whether the Circuit Court should have directed a verdict for the defendants on the ground that the insolvency of the defendant bank, occurring before the suit was filed, precluded the plaintiff from rescinding his stock subscription. It has become the settled rule in England since the decision in Oakes v. Turquand, L. R. 2 H. L. 325, 344, that a suit to rescind a stock subscription on the ground of fraud cannot be maintained by a stockholder, no matter what diligence he may have shown, after proceedings have been taken to liquidate the affairs

of the corporation, on the ground of its insolvency, inasmuch as the rights of creditors of the corporation, both as against the corporation and those who are registered shareholders, then become superior to the rights of the defrauded shareholder. Stone v. Bank, C. P. Div. 282, 307; Wright's case, 7 Ch. App. 60; Kent v. Brickmaking Co., 3 Ch. App. 493; Thomp. Corp. Sections 1439, 1441; Cook Stock & Stockh., Section 163.

"In this country there are some cases in which a stockholder's right to rescind his subscription after the intervention of proceedings in bankruptcy or after the insolvency of the corporation has been denied; but, as Mr. Thompson well remarks in his Commentaries on the Law of Corporations (Sec. 1449), it does not appear in any of the cases that the denial of the right to rescind was grounded exclusively on the fact that proceedings in bankruptcy had been instituted, or that the corporation had become insolvent. Farrar v. Walker, 3 Dill. 506, note, Fed. Cas. No. 4679; Upton v. Tribilcock, 91 U. S. 45; Ogilvie v. Insurance Co., 22 How. 381, 391; Michener v. Payson, Fed. Case No.9525; Duffield v. Ironworks 64 Mich. 293, 31 N. Y. 310; Turner v. Insurance Co., 65 Ga.649; Ruggles v. Brock, 6 Hun. 164; Hurd v. Kelly, 78 N. Y. 588; Howard v. Turner (Pa. Sup.) 26 Atl. 753. In all of these cases the evidence showed that there had either been some lack of diligence on the part of the stockholder in discovering the fraud of which he complained, or unreasonable delay in asserting his rights after the discovery of the fraud, or active participation in the management of the corporation, or that debts had been contracted by the corporation subsequent to the subscription, which either gave to corporate creditors superior equitable rights, or estopped the shareholders, as against a corporate creditor, from asserting that he was not a shareholder. The question whether a stockholder should be permitted to rescind his subscription, on the ground of fraud, after the insolvency of the company, is attended with much doubt and difficulty because of the peculiar relation which a shareholder sustains to the creditors of the company. In the case of Upton v. Englehart, 3 Dill. 496, 505, Fed. Case No. 16, 800, Judge Dillon, while discussing the subject, pointed out that the unbending English rule above referred to was influenced in a measure by the companies act (25 and 26 Vict. C. 89), which makes provision for a 'register of stockholders' to which the public have access, and that as no similar register of stockholders is ordinarily kept in the United States, the English decisions holding that the commencement of a proceeding to wind up a company, is in itself, a bar to a suit for a rescission, are not strictly applicable to the conditions which prevail here. He concluded the discussion of the question as follows:

" 'I am inclined to the opinion that if a company has fraudulently misrepresented or concealed material facts, and thus drawn an

innocent person into the purchase of stock—he at the time being guilty of no want of reasonable caution and judgment, and afterwards being guilty of no laches in discovering the fraud—and he thereupon, without delay, notifies the company that he repudiates the contract, and offers to rescind the purchase, these facts concurring, I am inclined to the opinion that the bankruptcy of the company, subsequently happening will not enable the assignee to insist that the purchase of stock is binding upon him.'

"There are obvious reasons why a shareholder of a corporation should not be released from his subscription to its capital stock after the insolvency of the company, and particularly after a proceeding has been inaugurated to liquidate its affairs, unless the case is one in which the stockholder has exercised due diligence, and in which no facts exist upon which corporate creditors can reasonably predicate an estoppel. When a corporation becomes bankrupt, the temptation to lay aside the garb of a stockholder on one pretense or another, and to assume the role of a creditor, is very strong, and all attempts of that kind should be viewed with suspicion. If a considerable period of time has elapsed since the subscription was made, if the subscriber has actually participated in the management of the affairs of the corporation, if there has been any want of diligence on the part of the stockholder, either in discovering the alleged fraud or in taking steps to rescind when the fraud was discovered; and, above all if any considerable amount of corporate indebtedness has been created since the subscription was made which is outstanding and unpaid—in all of these cases the right to rescind should be denied, where the attempt is not made until the corporation becomes insolvent. But if none of these conditions exist and the proof of the alleged fraud is clear, we think that a stockholder should be permitted to rescind his subscription as well after as before the company ceases to be a going concern. There is some force, doubtless, in the view which has sometimes been taken by eminent judges that when a person has been inveigled into making a stock subscription by representations that were clearly false and fraudulent, he should be entitled to rescind his subscription, even after the insolvency of the company, under the same circumstances that would entitle him to rescind a contract of a different nature; that is to say, by proof of due diligence in discovering the fraud, and of prompt action after it was discovered. Upton v. Tribilcock, 91 U. S. 55, 56; Duffield v. Ironworks (Mich.) 31 N. W. 310, 316. See also, Improvement Co. v. Merrill, 2 U. S. App. 434, 2 C. C. A. 629, and 52 Fed. 77."

The case of the Florida Land and Improvement Company v. Merrill et al., decided in the Circuit Court of Appeals, sixth circuit, and reported in the 52 Fed. Rep. p. 77, is a case very much in point. We quote the second point of the syllabus which reads as follows:

"When bank stock is fraudulently sold, and the proceeds are turned over to the bank, and a receiver is subsequently appointed, no creditor of the bank can be said to have any such interest in the proceeds as would prevent restitution and a rescission of the sale; and such appointment of a receiver does not, in itself, show that there are creditors of the bank who have prior equities."

This case again went to the Circuit Court of Appeals and is reported in 60 Fed. Rep. 17. We quote the head notes of this decision, which read as follows:

"An intending purchaser of bank stock is entitled to rely upon a statement of its president as to the bank's condition, without inquiring further.

"The receipt by a bank of the proceeds of a fraudulent sale of stock belonging to it, and the subsequent appointment of a receiver, give its creditors no such right in the proceeds as will prevent the purchaser from rescinding the sale and requiring restitution. 52 Fed. Rep. 77; 2 C. C. A. 629; 2 U. S. App. 434, reaffirmed."

We quote at length from the decision of the late Justice Jackson, in Winters v. Armstrong, *supra* (37 Fed. Rep. 509), as follows:

"The claim made by one of the counsel for the receiver, that his position as the representative of creditors is better than that of the Fidelity National Bank, and that he can enforce rights on behalf of creditors which would not exist in favor of the association, is not sound as applied to a case like the present. When the conclusion is reached that Winters, Strange and Woods are only to be regarded and treated as subscribers for valid stock which has not been, and cannot be, issued to them by the association, the receiver cannot, in behalf of either the bank, stockholders or creditors, enforce against them any right which the association could not itself have asserted. A receiver cannot enforce the payment of subscriptions to stock which the corporation could not have enforced at the time of his appointment. Cutting v. Damerel, 88 N. Y. 410. In respect to contracts of this character the receiver occupies no position superior to that of the bank for the reason that the corporate management, while in charge of its business, just as much as a receiver after his appointment, represents the interests of all persons, creditors as well as shareholders. When the corporation is insolvent the rights of creditors in respect to the corporate assets become most prominent and a receiver appointed to administer or collect such assets is regarded as more directly the representative of creditors. In a certain class of cases a receiver may assert rights which the corporation could not, thus he may disaffirm illegal and fraudulent transfers of

corporate property and may recover his funds and securities which have been misapplied. The governing officers of a corporation cannot, for example, release a stockholder or a subscriber for its stock, for his obligation to pay, to the prejudice of creditors. They cannot return to stockholders the capital stock of the corporation, which constitutes a trust fund for the benefit of creditors, to the injury of such creditors. They can make no fraudulent disposition of the corporate property for their private benefit, or for the benefit of the stockholders, leaving creditors unprovided for. These and like transactions involving the misapplication or fraudulent disposition of corporate property a receiver may disaffirm, and recover such assets for the benefit of creditors, when the corporation might not be in a position to do so. Wood v. Downer, 3 Mason 308; Curran v. Arkansas, 15 How. 304; Burke v. Smith, 16 Wall. 390; New Albany v. Burke, 11 Wall. 96, and Sawyer v. Hoag, 17 Wall. 619, afford illustrations of the cases in which receivers may assert rights which the corporation or corporate management could not enforce. But the present case involves no such principle. Subscribers to the new stock, which they have not, and cannot obtain, are in no sense the recipients of the corporate property or assets which have been fraudulently or wrongfully divested, misapplied, or disposed of to the prejudice of creditors. The rights and obligations growing out of these subscriptions rest upon contract, and in respect to such matters the receiver stands precisely in the shoes of the association and can only enforce what it could have enforced at the date of his appointment, and is subject, so far as the assets of the bank are concerned, to the same obligations as the bank would have been under had it continued in existence and never passed into the hands of the receiver. The Fidelity National Bank could not, under the facts stated, have enforced the payment of the notes executed by Woods and Strange; neither can the receiver do so. Winters could have recovered his deposit made on his subscription as against the association, and he is entitled to its allowance as a valid claim against the assets of the bank in the hands of the receiver, so far as anything disclosed by the pleadings appears."

In the case of Beale v. Dillon, decided by the Court of Appeals of Kansas, and reported in the 47 Pac. Rep. 317, the court determines the following proposition, as appears from the head notes of the case, reading as follows:

"An assignee at law of an insolvent corporation may maintain an action against a delinquent stockholder therein to collect an unpaid subscription to the capital stock of such corporation, and in such action the stockholder may interpose the defense that he was fraudulently induced to become a subscriber to the capital stock through the

false and fraudulent representations of the corporation and its officers."

This question was considered and passed upon by the United States Circuit Court of Appeals of the seventh circuit, in the case of Andrews v. National Foundry and Pipe Works, 22 C. C. A. 110, 76 Fed. Rep. 166, and the above decisions practically followed.

The position contended for was sustained by the Supreme Court of Missouri in the case of Haskell v. Worthington, 7 S. W. Rep. 481.

The same court, in the more recent case of Ramsey v. Thompson Mfg. Co. et al., 22 S. W. Rep. 719, reaffirmed this decision upon a review of all the authorities. In this last case, Justice Burgess, in delivering the opinion of the court, states the position of that court as follows:

"And while Mr. Cook says that the decided tendency of the decisions in this country is that corporate insolvency is a bar to such rescission, and the fact that the subscription was obtained by fraud and fraudulent representations, is not available as a defense in a suit against the subscriber to compel the payment of his stock, this court seems to have held otherwise in the case of Haskell v. Worthington, 94 Mo. 560, 7 S. W. Rep. 481. Brace, J., in delivering the opinion of the court in that case, which was an action by the assignee of a corporation upon a subscription to its capital stock, to recover the par value of the shares for which the defendant had subscribed, held that, as the assignee stood in the shoes of the corporation, it was a good defense to show that the corporation had entered into actual business with less capital stock subscribed than the amount stated in its articles of incorporation, the defendant not having by his conduct estopped himself from setting up the defense; that the assignee occupied no better position than the corporation did."

See also:

Whitney et al., v. Butler, 118 U. S., 655.

We quote at length from the opinion of Chief Justice Campbell in the case of Duffield v. E. G. Barnum Iron Works Co., 64 Mich., 293, as follows:

"The question seems to be narrowed to the inquiry whether plaintiff is deprived of his remedy by the subsequent assignment. If there was no fault in not discovering the wrong, and if the

suit was brought before any opposing claims had obtained a preference, it cannot be said there was any waiver, and it is difficult to see anything which can be treated as an estoppel. There is no foundation in reason or in law, so far as we can discover, for holding that he is debarred of complaint because others have also been subsequently defrauded. A creditor who becomes such by fraud in obtaining his money for one purpose, has as distinct an equity as those who were afterwards defrauded or persuaded into giving credit for goods or supplies. Under our statutes stockholders are not personally liable to contribute beyond what will pay up their stock, and creditors cannot enforce any rights, under the assignment, against paid-up stock at all. But the suit of plaintiff is based on the claim that he never was properly to be considered a stockholder by the company, and, under this assignment, if anything, had remained unpaid on his shares, it would have been as a balance collectible by the company as his subscription, and not a debt due to creditors themselves as such. In England the winding up process is mainly to enforce contribution from shareholders, upon the theory that credit is given them as such. But even there it is very clearly held that the distinction taken between defrauded stockholders who sue before winding-up proceedings, and those who delay until after, does not depend upon any principle of estoppel in favor of creditors acting in faith of their membership, but upon the legal position which they are placed in by the winding-up proceedings whereby all persons registered as shareholders become, by operation of law, bound to contribute, because those proceedings themselves fixed their status.

"This is very clearly explained in Stone v. City and County Bank, Ltd., 3 C. P., Div. 282; and in that same case, where the authorities are reviewed and explained, it was strongly intimated that while after the proceedings begun for winding up, the plaintiffs could not avoid being treated as shareholders, they might have sued in that capacity for the damages incurred by the fraud of the company, which induced them to buy stock, and been treated as creditors for the damages.

"In Smith's case, before cited, it was expressly decided that creditors had no better claim than defrauded shareholders to sue for redress, and could not be preferred to them under circumstances which did not fix a legal priority. Lord Cairns there remarks: 'It is one of the risks, and it ought to be known that it is one of the risks which creditors are liable to in dealing with limited companies, that it may turn out that some person whose name has been entered as a shareholder in the list has a right to have his name taken off the list if he can prove that it has been fradulently inserted there, and if he comes with promptitude to have the fraud redressed.' In other words, it is considered that, unless personally in the wrong in some way, all creditors stand on an equal footing for redress until, by some process, which the law has

authorized to have that effect, they are placed on a different footing; and, if this is so, any remedy which is seasonably resorted to must be sustained.

"It is the settled law of this state that a creditor who has obtained security by attachment or otherwise before a general assignment cannot be deprived of his preference by that or any other subsequent action of his debtor. If he was defrauded, it is equitable that he should have a remedy; and if he has not contributed himself to mislead other creditors, there is no legal provision in this state to prevent him from seeking it in the same way as if no other creditors existed. None of our corporation statutes create any such difference in ordinary cases. How far it is done in the specific cases of personal liability existing in some instances by constitutional or statutory provisions, we need not inquire. The present case is no such case, and the assignee, or the receiver who represents him, only holds the property and rights of the corporation, and not rights which the company itself could not enforce, except perhaps where property of the company has been fraudulently transferred. In this respect it varies considerably from the English winding-up acts. But as the suit here preceded the assignment, it would have been in season even there.

"In our opinion the plaintiff had a plain right to maintain his action based on the fraud complained of, and the court below erred in holding otherwise. The judgment must be reversed and a new trial ordered. If the funds representing the attached property and reserved for this case are sufficient, without impairing the claim in controversy, the costs will be paid out of that. If not, they will be paid like other legal charges by the receiver."

In the case of Robinson v. Dickey et al. (14 Tex. Civ. App. 70), this question is passed upon as follows:

"1. Plaintiff, induced by false representations made to him by the officers of a bank, that the bank was solvent, and that the shares of stock which were to be delivered to him as part consideration were worth their face value, contracted to convey certain lots to the bank, on its agreement to erect a building thereon. The bank never completed the contract, further than to deliver the stock, and subsequently went into the hands of a receiver. *Held*, that plaintiff was entitled to a rescission of the entire contract on tender of the stock itself to the receiver."

See also recent decision of the Court of Chancery of New Jersey in Tierney v. Parker, 44 Atl. R., 151.

We call attention to the recent decision of the Circuit Court of the 9th Circuit in the case of Stufflebeam v. De Lashmutt, 101 Fed., 367.

Also to the very able and clear review of the authorities upon this question made by Chief Justice Robinson, in the case of Savage v. Bartlett, etc., 78 Md., 561.

IV.

The somewhat recent decision of the court below (by a divided court) in the case of Scott v. Latimer (89 Fed. Rep., 843), changed the rule in the Eighth Circuit, and practically decided (in advance of their reaching that court) the cases at bar.

As we read the decision in Scott v. Latimer, it is mainly placed upon the ground:

That the liability of a stockholder, is not contractual, but entirely statutory, and that although the contract, by which the stock is acquired, be induced by fraud, the rescission of such contract, cannot release the liability imposed by the statute (regardless, we should say, whether a receiver had been appointed or not). This, fully appears, from the 2nd, and 3rd, points of the syllabi, in the case, but more clearly, from the following extracts taken from the opinion of the majority of the court:

"If it be true that the subscription to the stock was obtained by false representations touching the pecuniary condition of the bank, that did not make the contract absolutely void but only voidable at the option of the subscriber; and, therefore, when the bank was put in liquidation, the corporate creditors had the right to enforce the statutory liability against all persons who were then stockholders. * * *

"Suits of this character, strictly speaking, are not actions based upon the contract of subscription existing between the corporation and the stockholder. * * * The right of the creditors to enforce the statutory liability against shareholders in a national bank is not dependent upon the terms of the stock subscription contract. * * *

"The liability sought to be enforced in this case is not one created by contract existing between the corporation and its stockholders, but is one created by statute in favor of creditors, and not in favor of the corporation. And it is a liability which cannot be affected, discharged, or released by any action taken by the corporation, or by the combined action or agreement of the corporation and its stockholders. * * *

"It is thus made clear that the liability sought to be enforced in this case is not dependent upon the terms, or in fact upon the

existence, of a contract of subscription to the capital stock of the bank, but it is a liability imposed by statute in favor of creditors, and it is a liability, as already said, which cannot be modified or released by any action on the part of the corporation, or of the corporation and its stockholders. It is created for the benefit of the creditors, and no action on the part of the bank can estop the creditors from enforcing their rights in this particular. * * *

"As already said, this suit is not based upon the contract of subscription between the bank and the plaintiff in error, and is not, therefore, an action wherein the issue can be made as to the voidability of that contract, as between the bank and the shareholders. The suit is on behalf of the creditors to enforce the statutory liability, in which the bank has no interest; a liability which was not created by any contract to which the bank was a party; a liability which it is beyond the power of the bank to modify, release, or discharge: and a liability which, if once called into existence by the act of one assuming the position of a stockholder, cannot be defeated, save by the creditors, or some one acting in their behalf."

That the theory of the majority of the court in this case, that the contract of subscription or purchase has nothing to do with this liability is untenable, we have already seen.

We call attention of the court to the very vigorous, dissenting opinion of Justice Sanborn in this case, found on pages 856 to 865, quoting from it, as follows:

"It is held in those cases (the cases cited and relied upon by the majority of the court) that those who knowingly permit themselves in various ways to appear to be stockholders, those who were stockholders, but presented the false appearance that they were not, and those who fraudulently transferred their stock to irresponsible parties to escape liability, were estopped from defeating creditors of the corporation in their attempts to hold them as such. It is, indeed, repeatedly stated in those cases that the property of an insolvent corporation and the liability of the stockholder are a trust fund pledged for the benefit of the creditors; and that is equally true of every insolvent person. But in none of these cases —in no case cited by the court or counsel—was the holder of the stock duped into his place and liability by undiscoverable fraud. In none of them did any court hold that money obtained from, or liability imposed upon, a stockholder by fraud which he could not discover are a trust fund held for the benefit of the creditors of the corporation which perpetrated the fraud. Can a debtor by fraud confer upon his creditors any greater right to the property or liability of his victim than he gets himself? * * *

Why is not the right of one who is induced by fraudulent representations of a bank to buy its stock to a rescission of that sale

and a release of the liability it imposes superior to the claims of its creditors, or its receiver to enforce them? * * *

In all the cases cited by the majority either a valid contract of subscription of purchase existed, or the stockholders were estopped from rescinding a voidable contract, because they had acted as such after they knew, or might have known, the facts upon which they relied to avoid it. In the case at bar the contract was induced by fraud, and it was concealed by fraud. In this case no estoppel against the plaintiff in error can be sustained, because he did not know and could not learn the facts, and no duty to speak or act rested upon him until he acquired that knowledge, or means of knowledge.

The bank induced the plaintiff in error to play the part of a stockholder, and thereby to lose all the money he deposited with it, and to run the risk of liability to lose as much more by the same scheme of false representations of its solvency, of its flourishing condition, and of its increase of stock, which doubtless induced the creditor to take the bank's promise of repayment for the money he deposited with it. In such a case, why should not the right of the purchaser of stock who suffers the greater wrong be equal to that of the creditor who suffers less? Neither of them was aware of the fraud, neither of them did or could discover it until both were injured. Neither of them knowingly or negligently deceived the other, and, in my opinion, neither of them is entitled to estop the other from undoing the fraud from which they suffer."

See also, McClenathan v. I. L. & I. Co., (Va.), 30, S. E. R., 450.

V.

The decisions of the courts in England followed by the court below do not militate against the proposition stated. The leading case of Oakes v. Turquand (L. R. 2. H. L., 325), and the subsequent cases, are each and all based upon the provisions of the English Act of 1862, entitled, "An Act for the Incorporation, Regulation and Winding Up of Trading Companies and Other Associations" (Ch. 89, 25-26, Vict). See appendix, where some of the provisions are set out. This Act contains some 212 sections, collecting into one code the provisions which were thenceforth to be applicable to incorporations of the character provided for in the Act. By this Act, a public officer was appointed for keeping a register of, among other things, the name of the projected company; a statement of the nature of its intended business; the amount of its capital; the names and addresses of

every subscriber, with the number of shares taken by him and the amount paid on each share. It further provides that the register shall be open to inspection, not only of the members, but all other persons, and that any person, whose name has been wrongfully registered may apply to any Superior Court of law for equity for a rectification of the register. In the event of the company being wound up the Act provides that every member shall be liable to contribute to the assets of the company to an amount sufficient for the payment of its debts and liabilities.

Section 38 of the Act provides that shareholders within the preceding year, who have disposed of their shares, and are not registered at the time of the commencement of the winding up proceedings, shall, under certain circumstances and conditions, be liable to the payment of the debts, upon the winding-up of the corporation.

Shortly prior to the decision in Oakes v. Turquand, the House of Lords in the case of Railway Company v. Kisch (L. R. 2, H. L. 99), determined that one whose subscription to capital stock in an association was induced by fraud, had the right, upon the discovery of the fraud, to rescind his contract of purchase to the same extent as an individual would have the right in a contract between himself and another individual to rescind such contract for fraud.

Following this decision, came the case of Oakes v. Turquand, which we do not believe ever should have been construed as determining, under the Act, that the commencement of winding-up proceedings, against a corporation, cuts off the right of a shareholder, under any, and all circumstances, to rescind his contract, of subscription, and have his name removed from the register. This belief is strengthened by the head-notes to the case, a portion of which we quote as follows:

"Where a memorandum of association (which was registered) differed from the prospectus on which it professed to be founded, and on which as setting forth the true objects of the association, A, had become a shareholder, though he, on discovering the difference, might have repudiated his shares, he could not after the fail-

ure of the company, relieve himself from liability to contribute to the debts of the association, on the ground that he had been ignorant of something which, with proper diligence, he might have known."

"It is the duty of a person taking shares in a company to use reasonable diligence in making himself acquainted with the provisions of the memorandum of association. He must take the consequences of the negligence." * * * "A, applied, on the face of statements in the prospectus, for shares in a limited liability company. They were allotted. His name was put on the register of shareholders. At the end of nine months the company failed. It was ordered to be wound up. A, then applied to have his name removed from the list of contributories;

"*Held*, affirming the decision of Malins, V. C., that it was properly placed there."

Conceding, however, for the sake of the argument, that this case, is as broad, as it has been construed to be, by some courts, and some text-writers, yet, it ought not to be an authority, in a case like the one at bar, as there are many notable distinctions, between the English Act, and the Acts of Congress, concerning national banks, some of which we call the court's attention to as follows:

There is no requirement in the national banking acts, that one, having a right from any cause, to have his name removed from the registered list of stockholders shall proceed, in a court, to compel the taking of his name, from the register. It must be conceded, that a shareholder, in a national bank, induced to become such by the fraud of the bank, may, while it is a going concern, make a common law rescission, of his contract of purchase, and relieve himself from all liability.

Whitney v. Butler, *supra*.

Neither is there any provision for a public registry of names of the shareholders, in any national bank, which may be examined, by the public at large, or by any one, who intends becoming a creditor of such bank. The provisions of Sec. 5210, R. S., after providing for the keeping of a list of the shareholders, with the names and residences, provides:

"Such list shall be subject to the inspection of all the shareholders and creditors of the association and the officers authorized

to assess taxes under state authority, during the business hours of each day in which business may be legally transacted. A copy of such list on the first Monday of July of each year, verified by the oath of such president or cashier, shall be transmitted to the comptroller of the currency."

As we have seen, there is no act of Congress which places a receiver appointed for a national bank, in any better position, as to the assets of the bank, than would the assignee of an individual insolvent for the benefit of creditors, be placed in, by the rules of the common law.

VI.

While some text-writers, and some courts, cite the decision, of this court, in Upton v. Tribilcock (91 U. S. 45), as a decision, supporting the supposed doctrine of Oakes v. Turquand, a careful examination of the opinion in the case will lead to the conclusion, that it is not an authority sustaining such view. The action in that case, was brought by the assignee of an insolvent company, to recover a stock subscription, and the defense was, that the subscription, had been procured by the false representations of the agent of the company. This court held, that these representations were, if anything, a misrepresentation as to the law, and were not misrepresentations as to the facts, and hence not the basis of a right to a rescission of the contract for fraud; but that if the representations, amounted to such fraud, as would give to the defendant, in that case, the right of rescission, he had been guilty of *laches* in ascertaining the truth, or falsity of the representations, and especially guilty of *laches* in repudiating the contract of subscription. The right of the defendant in that case to repudiate the contract of subscription on the ground of fraud, apart from the question of *laches* on his part, even after the assignment, and the right to repudiate it, without a proceeding against the company to remove his name from the books of the company, is distinctly recognized by this court in that case, and there is no intimation by the court, in its opinion that it was too late after the assignment, to rescind the contract of subscription. It seems to have been conceded, by the court,

that such a rescission could be made, had the defendant in that case, grounds for making the same, and had exercised the right promptly, without any *laches*.

The few other cases in other jurisdictions supporting the English doctrine do so solely on authority of the English cases, and upon the erroneous proposition that the liability is purely statutory and not contractual.

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## THIRD POINT.

**The court below erred in affirming the ruling of the Circuit Court sustaining each of the demurrers to each of the cross-petitions.**

I.

Each of these answers included in addition to the defenses referred to, a cross-petition, against the receiver (based upon the facts stated in each of the separate defenses), to recover a judgment for the amount paid to the bank for this stock asking that such judgment, when recovered, be paid by the receiver out of the funds in his hands, pro rata. The right to set up these counter-claims, in the answers, is given by sections 94 and 95 of the Kansas code stating what an answer can contain.

Section 94 * * *

"A statement of any new matter constituting a defense, counter-claim or set-off, or a right to relief concerning the subject of the action, in ordinary and concise language, and without repetition."

Section 95 reads as follows:

"The counter-claim mentioned in the last section must be one existing in favor of a defendant and against a plaintiff between whom a several judgment might be had in the action, and arising out of the contract or transaction set forth in the petition as the foundation of plaintiff's claim, or connected with the subject of the action. * * *"

The facts stated in this cross-petition, under the decisions of the Supreme Court of Kansas creates a counter-claim that can be used as a set-off.

In the case of Fanston v. Linsley, 20 Kas. 235, the second and third points of the syllabus, are as follows:

"2. *When tort may be waived; benefit to wrongdoer.* Whenever one person commits a wrong or tort against the estate of another, with the intention of benefitting his own estate, the law will, at the election of the party injured, *imply* or presume a contract on the part of the wrongdoer to pay to the party injured the full value of all benefits resulting to such wrongdoer. And when the injured party elects to waive the tort, his cause of action may be used as a set-off.

"3. *When a tort may not be waived; naked trespass.* Where one person commits a wrong or tort against another, without any intention of benefiting his own estate, and his own estate is not thereby benefited, the law will not imply or presume a contract on the part of such wrongdoer to pay for the resulting damages; and such cause of action cannot be used as a set-off."

This decision has been repeatedly affirmed.

St. L. F. S. & W. R. R. Co. v. Chenault et al., 36 Kas. 51;

Smith v. McCarthy, 39 Kas. 308;

Frankhouser v. Neally, 54 Kas. 744;

In Smith v. McCarthy, *supra*, the first and second points of the syllabus read as follows:

"Where a person takes and sells the property of another, the owner may elect to waive the tort and sue upon the implied contract for the value of the same; and whether he has so elected, and the nature of the action brought, are to be determined by the court from the pleadings."

"In determining the effect of pleadings, they should be liberally construed with a view to substantial justice between the parties; and the pleadings herein are examined and are held to state a cause of action *ex contractu*."

In this case, it was held that the following allegations stated a cause of action on an implied promise:

"The plaintiff avers that on the first day of October, 1885, one Jerry McCarthy, being at that time indebted to this plaintiff in the sum of nine hundred and twenty-five dollars, made, executed and

delivered to the plaintiff his certain chattel mortgage in writing, a copy of which, with all the indorsements thereon, is attached hereto, marked 'Exhibit A,' and made a part of this petition; that said chattel mortgage was forthwith, on the delivery of the same, deposited by the plaintiff in the office of the register of deeds of Atchison county, Kansas, where said chattel property was situated and the mortgagor resided; that on or about the 28th day of October, 1885, and while said chattel mortgage was in full force and effect, of record, and unpaid, the defendant, by and through her duly authorized and appointed agent, Ryan Smith, did take the fifty head of hogs mentioned and described in 'Exhibit A,' from the possession of the plaintiff mortgagor, Jerry McCarthy, without his consent, and without the consent of this plaintiff, and did convert the same to her own use and benefit; that the value of said fifty hogs was at said time, and now is, the sum of seven dollars a head, all of said hogs being of the value of three hundred and fifty dollars; that the plaintiff has duly demanded from the defendant the said hogs and all of them, which demand was refused; and that he also demanded the value of said hogs, to wit, the sum of $350, of and from defendant, which demand has been refused; that the plaintiff has a special ownership in and to said hogs to the amount of $925, being the amount of the chattel mortgage hereto attached. Wherefore, the plaintiff prays judgment against defendant for three hundred and fifty dollars, and costs of this action."

II.

We have difficulty in understanding the position of the court below with reference to these cross-petitions (Pr. tr., p. 31, term No. 180). That each of the plaintiffs in error had a claim good as against the bank, as for money had and received, must be conceded.

> Central Transportation Co. v. Pullman's Palace Car Co., 171 U. S., 138.

That such a claim was entitled to be established as a claim which was entitled to participation in the distribution of the assets must also be conceded.

> Chemical National Bank of Chicago v. Hartford Deposit Co., 161 U. S. 1.

There being claims against the bank, the plaintiffs in error could, if they chose, bring suit directly against the receiver to establish the same as claims entitled to share in all distribution.

Southern Exp. Co. v. Western N. C. R. R. Co., 99 U. S., 191;

Denton v. Baker (U. S. C. C. A., 9th Circuit), 79 Fed., 189.

Speckart et al. v. German National Bank et al., 85 Fed. 12.

While it is clear that these claims grew out of an implied contract, yet if they grew out of a tort, there is no reason existing, why they should not be paid pro rata with all other claims, or be used as a set-off to the extent that they are entitled to participate in the assets in an action of this character. While, of course, the establishment of these claims could only determine their right to receive the pro rata share in the distribution, yet to that extent they should be allowed as a set-off.

Scammon v. Kimball, 92 U. S., 362;

Carr v. Hamilton, 129 U. S., 252;

Scott v. Armstrong, 146 U. S., 499, *supra;* and cases cited;

Central Appalachian Co., et al., v. Buchanan (C. C. A. 6 Cir.) 90 Fed. Rep., 454, and cases cited.

III.

There is no conceivable view that can be taken of the facts stated in the cross-complaints which would not entitle the plaintiffs in error to a judgment against the receiver for the amount of each of their several claims, or the right to set the amount of such claims off *pro tanto* against any claim of the receiver, under the Kansas statute, *supra*.

It must be conceded that under the provisions of section 2334 revised statutes, and the decisions of this court (collated in Denton v. Baker, *supra*), that Hood, and Lantry, each, had claims against the Missouri National Bank at the time it was placed in the hands of the receiver, growing out of the admitted fraud of the bank in selling the stock it sold to them, whether they severally were, and are, stockholders, so far as the receiver is concerned, or not; or whether they be regarded as people who having been stockholders, ceased being such from the time of the attempted rescission of

their contract of purchase, or whether they be regarded as persons who purchased over issued stock, and, therefore, never were stockholders. If they never acquired any stock, owing to the fact that the transaction was *ultra vires,* or if they rescinded the contract of purchase of the stock rightfully, they each had a several claim against the bank for the amount of money which they paid for the stock, which can be enforced in this action as a counter-claim if such claims grew out of the same transaction as did the contract which the receiver is trying to enforce against each of them. On the other hand, if the receiver has the right to recover from them the assessments ordered by the comptroller, either upon the theory that they are estopped as to him, to deny the fact that they are stockholders, or that they have waived the right to deny that they are stockholders, by reason of their laches, or that after the insolvency of the bank and the appointment of the receiver it is too late, as to the receiver, to rescind the contract of purchase, or deny the fact of their being stockholders for any reason, such right of recovery would not, in any wise, interfere with the right of action on behalf of each of the plaintiffs in error against the bank on account of its fraud, as this right existed (whether plaintiffs in error knew it or not) at the time the bank was placed in the hands of the receiver. Plaintiffs in error have the right to establish these claims against the bank either by a judgment of the court, or by the allowance of the receiver, under the provisions of section 2334, revised statutes [see Denton v. Baker, *supra,* and authorities there cited], and these claims can, in such case, be used as a set-off if it be held that they do not grow out of the same transaction involved in the matters set out in the petition.

The receiver, if he can recover at all, will recover because of the contract made between the plaintiffs in error and the bank for the benefit of the creditors of the bank, by the contract of purchase of this stock from the bank. If the plaintiffs in error have the several rights to recover against the bank it is on account of their claims that grew out of the transaction of this purchase, upon which the

right of the receiver is based, and consequently, it falls within the provisions of the Kansas code relative to counter-claims.

For the convenience of the court, we have placed in the appendix copies of those portions of the National Bank Acts applicable to the case, and also some of the sections of the English Act of 25-26 Victoria, referred to.

All of which we respectfully submit.

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# APPENDIX.

The following are all the sections of the Revised Statutes in reference to national banks having any application to the case under consideration:

"Sec. 5139. The capital stock of each association shall be divided into shares of $100 each, and be deemed personal property, and transferable on the books of the association in such manner as may be prescribed in the by-laws or articles of association. Every person becoming a shareholder by such transfer shall, in proportion to his shares, succeed to all the rights and liabilities of the prior holder of such shares; and no change shall be made in the articles of association by which the rights, remedies, or security of the existing creditors of the association shall be impaired."

"Sec. 5151. The shareholders of every national banking association shall be held individually responsible, equally and ratably, and not one for another, for all contracts, debts, and engagements of such association, to the extent of the amount of their stock therein, at the par value thereof, in addition to the amount invested in such shares."

"Sec. 5210. The president and cashier of every national banking association shall cause to be kept at all times a full and correct list of the names and residences of all the shareholders in the association, and the number of shares held by each, in the office where its business is transacted. Such list shall be subject to the inspection of all the shareholders and creditors of the association, and the officers authorized to assess taxes under state authority, during business hours of each day in which business may be legally transacted. A copy of such list on the first Monday of July of each year, verified by the oath of such president or cashier, shall be transmitted to the Comptroller of the Currency."

"Sec. 5234. On becoming satisfied, as specified in section-fifty-two hundred and twenty-six and fifty-two hundred and twentys seven, that any association has refused to pay its circulating notes as therein mentioned, and is in default, the Comptroller of the Currency may forthwith appoint a receiver, and require of him such bond and security as he deems proper. Such receiver, under the direction of the comptroller, shall take possession of the books, records, and assets of every description of such association, collect

all debts, dues and claims belonging to it, and, upon the order of a court of record of competent jurisdiction, may sell or compound all bad or doubtful debts, and, on a like order, may sell all the real and personal property of such association, on such terms as the court shall direct; and may, if necessary to pay the debts of such association, enforce the individual liability of the stockholders. Such receiver shall pay over all money so made to the treasurer of the United States, subject to the order of the comptroller, and also make report to the comptroller of all his acts and proceedings."

"Sec. 5235. The comptroller shall, upon appointing a receiver, cause notice to be given, by advertisement in such newspapers as he may direct, for three consecutive months, calling on all persons who may have claims against such association to present the same, and to make legal proof thereof."

"Sec. 5236. From time to time, after full provision has been first made for refunding to the United States any deficiency in redeeming the notes of such association, the comptroller shall make a ratable dividend of the money so paid over to him by such receiver on all such claims as may have been proved to his satisfaction or adjudicated in a court of competent jurisdiction, and, as the proceeds of the assets of such association are paid over to him, shall make further dividends on all claims previously proved or adjudicated; and the remainder of the proceeds, if any, shall be paid over to the shareholders of such association, or their legal representatives, in proportion to the stock by them respectively held."

Chapter 89 of Statutes 25–26, Victoria, enacted August 7, 1862, entitled "An Act for the incorporation, regulation and winding-up of trading companies and other associations," provided for the incorporation of trading associations, etc. The 18th, 23rd, 35th, 38th, 74th and 82d sections of the Act are, for the convenience of the court, here copied and set out:

18. Upon the registration of the Memorandum of Association, and of the Articles of Association in cases where articles of association are required by this Act, or by the desire of the parties to be registered, the registrar shall certify, under his hand that the company is incorporated, and in the case of a limited company, that the company is limited. The subscribers of the Memorandum of Association, together with such other persons as may from time to time become members of the company, shall thereupon be a body corporate by the name contained in the memorandum of association, capable forthwith of exercising all the functions of an

incorporated company, and having perpetual succession and a common seal, with power to hold lands, but with such liability on the part of the members to contribute to the assets of the company in the event of the same being wound up, as is hereinafter mentioned. A certificate of the incorporation of any company given by the Registrar, shall be conclusive evidence that all the requisitions of this Act in respect of registration have been complied with.

23. The subscribers of the Memorandum of Association of any company under this Act shall be deemed to have agreed to become members of the company whose memorandum they have subscribed, and upon the registration of the company shall be entered as members on the register of members hereinafter mentioned; and every other person who has agreed to become a member of a company under this Act, and whose name is entered on the register of members, shall be deemed to be a member of the company.

35. If the name of any person is, without sufficient cause, entered in or omitted from the register of members of any company under this Act, or if default is made, or unnecessary delay takes place in entering on the register the fact of any person having ceased to be a member of the company, the person or member aggrieved, or any member of the company, or the company itself, may, as respects companies registered in *England* or *Ireland*, by motion in any of Her Majesty's Superior Courts of Law or Equity, or by application to a Judge sitting in Chambers, or to the Vice-Warden of the Stannaries in the case of companies subject to his jurisdiction, and as respects companies registered in *Scotland* by summary petition to the court of Session, or in such other manner as the said courts may direct, apply for an order of the court that the register may be rectified; and the court may either refuse such application, with or without costs, to be paid by the applicant, or it may, if satisfied of the justice of the case, make an order for the rectification of the register, and may direct the company to pay all the costs of such motion, application or petition, and any damages the party aggrieved may have sustained. The court may in any proceeding under this section decide on any question relating to the title of any person who is a party to such proceeding to have his name entered in or omitted from the register, whether such question arises between two or more members or alleged members, or between any members or alleged members and the company, and generally the court may in any such proceeding decide any question that it may be necessary or expedient to decide for the rectification of the register; provided that the court, if a court of common law, may direct an issue to be tried, in which any question of law may be raised, and a writ of error or appeal,

in the manner directed by "The Common Law Procedure Act, 1854," shall lie.

38. In the event of a company formed under this Act being wound-up, every present and past member of such company shall be liable to contribute to the assets of the company to an amount sufficient for payment of the debts and liabilities of the company, and the costs, charges and expenses of the winding-up, and for the payment of such sums as may be required for the adjustment of the rights of the contributories amongst themselves, with the qualifications following; (that is to say):

(1) No past member shall be liable to contribute to the assets of the company if he has ceased to be a member for a period of one year or upwards prior to the commencement of the winding-up.

(2) No past member shall be liable to contribute in respect of any debt or liability of the company contracted after the time at which he ceased to be a member.

(3) No past member shall be liable to contribute to the assets of the company, unless it appears to the court that the existing members are unable to satisfy the contributions required to be made by them in pursuance of this Act.

(4) In the case of a company limited by shares, no contribution shall be required from any member exceeding the amount, if any, unpaid on the shares in respect of which he is liable as a present or past member.

(5) In the case of a company limited by guarantee, no contribution shall be required from any member exceeding the amount of the undertaking entered into on his behalf by the Memorandum of Association.

(6) Nothing in this Act contained shall invalidate any provision contained in any policy of insurance or other contract whereby the liability of individual members upon any such policy or contract is restricted, or whereby the funds of the company are alone made liable in respect of such policy or contract.

(7) No sum due to any member of a company, in his character of a member, by way of dividends, profits, or otherwise, shall be deemed to be a debt of the company payable to such member in a case of competition between himself and any other creditor not being a member of the company; but any such sum may be taken into account for the purposes of the final adjustment of the rights of the contributories amongst themselves.

74. The term "Contributory" shall mean every person liable to contribute to the assets of a company under this Act, in the event of the same being wound up. It shall also in all proceed-

ings for determining the persons who are to be deemed contributories, and in all proceedings prior to the final determination of such persons, include any person alleged to be a contributory.

82. Any application to the court for the winding-up of a company under this Act shall be by petition; it may be presented by the company, or by any one or more creditor or creditors, contributory or contributories of the company, or by all or any of the above parties, together or separately; and every order which may be made on any such petition shall operate in favor of all the creditors and all the contributories of the company in the same manner as if it had been made upon the joint petition of a creditor and a contributory.